Chapter Three

Spending Options

Savings for most of the nondefense discretionary spending options in this chapter are estimated in two ways: relative to the freeze variation of the Congressional Budget Office's baseline, referred to as WODI (without discretionary inflation), and relative to the inflation-adjusted version, or WIDI (with discretionary inflation). Savings for most of the defense options are estimated relative to program levels that are assumed to be roughly the same under WODI or WIDI.

050

National Defense

Budget function 050 comprises spending for national defense. Although 95 percent of that spending falls within the Department of Defense, function 050 also includes the atomic energy activities of the Department of Energy and smaller amounts in the budgets of other federal departments and agencies. CBO estimates that discretionary outlays for function 050 will be about $283 billion in 2000. Mandatory spending in that function usually shows negative balances because of payments made to federal agencies. (In 1991, those receipts were unusually large because of reimbursements by foreign governments for some of the costs of the Persian Gulf War.) CBO's estimate of increased outlays for 2000 would mark the second consecutive year of nominal growth in defense spending.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	303.9	332.2	299.1	276.1	262.2	262.9	265.0	266.2	272.4	288.1	289.9
Outlays											
Discretionary	300.1	319.7	302.6	292.4	282.3	273.6	266.0	271.7	270.2	275.5	283.0
Mandatory	-0.8	-46.4	-4.3	-1.3	-0.6	-1.5	-0.2	-1.2	-1.8	-0.6	-1.0
Total	299.3	273.3	298.4	291.1	281.6	272.1	265.8	270.5	268.5	274.9	282.0
Memorandum:											
Annual Percentage Change in Discretionary Outlays		6.5	-5.3	-3.4	-3.5	-3.1	-2.8	2.1	-0.5	1.9	2.7

050-01-A Reduce U.S. Forces to START II Levels by 2007

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	0	0
2003	0	0
2004	0	0
2005	20	10
2001-2005	20	10
2001-2010	920	840

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-01-B and 050-02

RELATED CBO PUBLICATION:

Letter to the Honorable Thomas A. Daschle regarding the estimated budgetary impacts of alternative levels of strategic forces, March 18, 1998.

The second Strategic Arms Reduction Treaty (START II) will require the United States to cut its long-range nuclear forces to 3,500 warheads by 2003—roughly one-third of the 1990 level. START II was ratified by the Senate in 1996, but it faces an uncertain future in Russia's parliament, the Duma. Presidents Clinton and Yeltsin agreed to delay full implementation of the treaty until December 31, 2007, in an effort to encourage ratification by the Duma. However, the forces to be dismantled by that date must be made inoperable by the end of 2003.

Today's forces remain largely consistent with the START I treaty—500 Minuteman III intercontinental ballistic missiles (ICBMs) with three warheads each; 50 Peacekeeper ICBMs with 10 warheads each; 18 Trident submarines (each carrying 192 warheads on 24 missiles); and 94 B-52H, 94 B-1B, and 21 B-2 bombers. The Administration would achieve the 3,500-warhead limit in START II by eliminating all 50 Peacekeepers, four Trident submarines, and 23 B-52H bombers by the end of 2007. It would also reduce the number of warheads on Minuteman III missiles from three to one and on Trident D5 missiles from eight to five and redesignate its B-1B bombers as conventional bombers. Although the Administration has decided to eliminate the four Trident submarines over the next five years to save money, it plans to keep all 50 Peacekeeper missiles and 94 B-52Hs in the force until the Duma ratifies START II.

This option would reduce U.S. forces to START II levels even if the Duma does not ratify the treaty. Those cuts would be made by the end of 2007, the treaty's modified implementation date. The primary motivation would be financial; those changes would save $920 million through 2010 relative to the Administration's plans. All of the savings would come from not having to operate Peacekeeper missiles after 2007. (There would be no savings from retiring the 23 B-52Hs because the Administration does not operate them today.) Savings could be $750 million higher through 2010 if the forces were retired by 2003, the original implementation date for START II. If the Duma never ratifies START II and the Air Force is required to keep Peacekeeper in the force beyond 2010—when it will run out of missiles for test flights—there would be significant costs associated with either reestablishing the Peacekeeper production line or developing a replacement missile. Compared with that possibility, this option might save several hundred million dollars through 2010.

Supporters of this approach argue that keeping long-range forces at today's levels is unnecessary. According to several reports, Russia will have trouble maintaining its forces at START I levels. Many of its missiles and submarines are nearing the end of their service life, and production of replacements has slowed to a trickle or stopped altogether. For that reason, several prominent former opponents of START II in the Duma have recently urged ratification. Some advocates of this option also argue that adopting it will encourage the Duma to ratify the treaty.

Critics argue that U.S. forces should remain at START I levels. They oppose any unilateral disarmament. They also worry that Russia might build up its nuclear forces if a hard-line government came to power. In their view, the Duma will only ratify the treaty if it is faced with a robust U.S. START I force.

050-01-B Reduce Nuclear Delivery Systems Within Overall Limits of START II

	Savings (Millions of dollars) Budget Authority	Outlays
2001	670	240
2002	420	340
2003	620	440
2004	690	540
2005	830	710
2001-2005	3,230	2,270
2001-2010	8,330	7,880

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-01-A and 050-02

RELATED CBO PUBLICATION:

Letter to the Honorable Thomas A. Daschle regarding the estimated budgetary impacts of alternative levels of strategic forces, March 18, 1998.

This option would go one step farther than the previous alternative (050-01-A). It would reduce the number of missiles and submarines below the levels planned by the Administration for START II but keep the number of warheads at START II levels. Specifically, it would retire four additional Trident submarines and 200 Minuteman III intercontinental ballistic missiles by 2003, retaining 10 Tridents and 300 Minuteman IIIs. To keep the same number of warheads, the smaller Trident force would carry seven warheads on each missile instead of five (see option 050-02). Minuteman III missiles would carry one warhead. This option would keep the same number of nuclear bombers as option 050-01-A, each carrying an average of 16 warheads. In all, those forces would carry nearly 3,500 warheads—the limit set in START II.

Compared with keeping U.S. forces at START I levels, this option would save $670 million in 2001 and $8.3 billion through 2010. One-fifth of those savings—which were outlined in option 050-01-A—would come from reducing forces to the START II levels planned by the Administration and thus do not represent savings from the Administration's budget plan. However, this option would save an additional $670 million in 2001 and $7.4 billion through 2010 compared with the Administration's plan: $3.1 billion from reduced operation and support costs (from retiring 200 Minuteman ICBMs and four additional Trident submarines) and $4.3 billion from lower levels of investment spending (from canceling production of the D5 missile after buying 12 in 2000, extending the service life of fewer Minuteman missiles, and forgoing the Administration's plans to reconfigure four Trident submarines under START II so they can carry new D5 missiles).

During the Cold War, this option might have raised concerns about stability. By putting more nuclear "eggs" in fewer baskets, the United States would have increased its vulnerability to a surprise attack. But today those concerns are less acute. The United States may now decide that it can save money safely by deploying its warheads on fewer weapon systems. Moreover, this option would retain three types of nuclear systems—the so-called nuclear triad—and thus provide a margin of security against an adversary's developing a new technology that would render other legs of the triad more vulnerable to attack.

The disadvantages of this option include those raised in option 050-01-A about cutting forces below START I levels before Russia ratifies START II. In addition, carrying more warheads on D5 missiles would reduce the targeting flexibility of U.S. planners, and deploying fewer submarines might increase their vulnerability to Russian antisubmarine forces. Unilaterally cutting forces would also limit the United States' ability to increase the number of warheads it deployed if Russia decided not to abide by START II. Indeed, some critics argue that unilateral cuts would reduce U.S. leverage to get Russia to ratify START II. Supporters of this option, however, counter that U.S. cuts would encourage ratification because they would reduce the United States' potential to break out of START II—one of Russia's major concerns about the treaty.

050-02 Terminate Production of D5 Missiles After 2000

	Savings (Millions of dollars) Budget Authority	Outlays
2001	670	240
2002	420	340
2003	620	440
2004	690	540
2005	920	780
2001-2005	3,320	2,340
2001-2010	4,870	4,710

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-01-A and 050-01-B

RELATED CBO PUBLICATION:

Rethinking the Trident Force (Study), July 1993.

Under both Strategic Arms Reduction Treaties (START I and II), the Navy plans to deploy a force of 14 Trident submarines. Each one will carry 24 D5 missiles—the most accurate and powerful submarine-launched ballistic missile (SLBM) in the U.S. inventory. Today, the Navy has 10 Trident submarines armed with D5s and eight armed with older C4 missiles. To keep 14 submarines, it must convert four older subs to carry D5s as well. To arm that force, CBO estimates, the Navy will have to purchase a total of 425 D5 missiles, 372 of which it has already bought. If Russia ratifies START II, the Administration will probably cut the number of warheads on each missile from eight to five (for a total of 1,680) to keep the number of U.S. warheads near the ceiling allowed by that treaty.

This option would terminate production of D5 missiles after 2000 and retire all eight C4 submarines by 2005. The Navy would then have 372 D5s—25 more than it says it needs to support a 10-submarine force. Like the Administration's plan for START II, this option would wait to retire the C4 submarines to encourage Russian compliance with START II and to give the United States flexibility to stay at higher START I levels if Russia does not comply. To retain 1,680 warheads, the option would increase the number of warheads on each D5 missile from five to seven.

Compared with the Administration's plan for START I and II, this option would save $670 million in 2001 and $4.9 billion through 2010. The savings would come from canceling missile production ($2.6 billion), retiring all eight C4 submarines rather than upgrading four of them ($1.1 billion), and operating fewer subs ($1.2 billion).

Terminating production of the D5 would have several drawbacks. Loading more warheads on existing missiles would reduce their range by roughly 20 percent, limiting the areas in which submarines could operate. It would also reduce the flexibility of the force, since missiles with fewer warheads can cover more widely dispersed targets. Deploying D5 missiles with seven warheads would also constrain the United States' ability to expand its SLBM force by adding back the extra warheads if Russia violated or never ratified START II. In addition, reducing the fleet to 10 submarines could increase its vulnerability to attack by Russian antisubmarine forces.

Nevertheless, some people may consider the capability retained under this option sufficient to deter nuclear war. Although the missiles' range and the submarines' patrol areas would be smaller, they would still exceed the levels planned during the Cold War—when Russia had more antisubmarine forces and the United States intended to deploy the D5 with eight large warheads (W-88s). Moreover, less targeting flexibility might not reduce the nuclear deterrent: 1,680 warheads deployed on 336 missiles might not deter an adversary any more than if they were on the 240 missiles called for in this option. Also, the smaller likelihood of nuclear war and Russia's atrophying nuclear forces may have weakened the rationale for the United States to be able to increase its forces rapidly by adding warheads to the D5. In fact, since the U.S. ability to do that is one of Russia's biggest concerns about START II, adopting this option could make passage of the treaty more likely.

050-03 Reduce the Scope of DOE's Stockpile Stewardship Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	50	40
2002	120	100
2003	200	170
2004	280	250
2005	340	310
2001-2005	990	870
2001-2010	2,790	2,650

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATION:

Preserving the Nuclear Weapons Stockpile Under a Comprehensive Test Ban (Paper), May 1997.

The Department of Energy (DOE) has developed the Stockpile Stewardship Program to preserve the long-term reliability and safety of U.S. nuclear weapons without testing them by exploding them underground. To carry out the program, DOE plans to continue operating both of its weapons-design laboratories (Los Alamos and Lawrence Livermore) and its engineering lab (Sandia). It will also construct several new facilities to provide data on the reliability and safety of nuclear weapons as they age. In addition, DOE will conduct "zero-yield" subcritical tests at the Nevada Test Site so it can keep enough skilled technicians there to be able to resume testing nuclear weapons by exploding them underground if the United States decides that doing so is in the national interest—a capability that the President has ordered DOE to retain.

DOE plans to spend an average of $2.5 billion a year over the next 10 years on what has historically been known as weapons research, development, and testing. To some observers, a budget of that size today is excessive and unnecessary.

This option would reduce the scope of the stewardship program by consolidating the two design laboratories and halting all testing activities at the Nevada Test Site. However, it would preserve the other elements of the stewardship program, including the Dual-Axis Radiographic Hydrotest (DARHT) facility at Los Alamos and the National Ignition Facility (NIF) at Lawrence Livermore. Taken together, the changes in this option would reduce employment by about 2,000 people. They would also save $50 million in 2001 and $2.8 billion through 2010 compared with the Administration's 2000 budget.

Those savings assume that weapons-design activities would be consolidated over five years at Los Alamos, which developed most of the weapons that are likely to remain in the stockpile. Lawrence Livermore's primary focus would become other scientific research. To ensure that the warheads it developed could be reliably maintained, some designers from Lawrence Livermore would be relocated to Los Alamos. However, a cadre of weapons scientists would remain at Livermore to act as an independent review team for Los Alamos's efforts. To provide them with challenging work, Livermore would keep large computational facilities for modeling the complex processes inside nuclear weapons and would build NIF as currently planned. (Alternatively, stewardship activities could be consolidated at Lawrence Livermore, but the savings would be lower.)

To some people, this option would cut the planned stewardship program too deeply. They believe that the program is the minimum effort necessary to maintain the nuclear stockpile without underground testing. In their view, scientists will need new facilities to obtain data on reliability that were formerly provided directly by such testing. They also contend that consolidation would reduce competition and peer review, result in the loss of some facilities that could not easily be transferred, and eliminate Lawrence Livermore's central unifying mission (and thus its motivation for excellence). For those reasons, the President has directed DOE to retain both labs. Closing the Nevada Test Site would increase the time needed to resume underground testing if Russia started a new arms race or the United States discovered a serious problem with its stockpile that could only be corrected by testing. Closing the test site would also stop scientists from conducting subcritical experiments to learn more about how aging affects the plutonium components in nuclear weapons.

To other people, this option would not cut deeply enough. In their view, keeping part of a second lab and building DARHT and the $1.2 billion NIF are unnecessary to support the nuclear stockpile. Furthermore, they claim, those facilities might allow DOE scientists to continue designing and testing weapons and circumvent the restrictions imposed by the Comprehensive Test Ban Treaty. Even if DOE has no such intentions, the perception of such a capability could make it difficult to convince countries such as India, which are critical of the United States' plans to preserve its nuclear weapons under a test ban, that the United States has really given up designing new weapons. Critics also argue that NIF should be funded outside the nuclear weapons program if it can help scientists understand how to harness fusion for civilian energy, as supporters claim.

Finally, some analysts are fundamentally opposed to a U.S. moratorium on testing (which will become permanent if the United States ratifies the test ban treaty). They contend that the only way to ensure the reliability of U.S. nuclear weapons is to explode those weapons underground. They also worry that by halting the development and testing of new types of weapons, the United States will lose the skilled people necessary to preserve the stockpile. This option does not address the test ban directly, but the cuts it would make to the laboratories would probably be resisted by test-ban opponents.

050-04 Eliminate Two Army National Guard Combat Divisions

	Savings (Millions of dollars) Budget Authority	Outlays
2001	247	218
2002	510	473
2003	527	516
2004	544	536
2005	561	554
2001-2005	2,389	2,296
2001-2010	5,460	5,325

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATIONS:

Making Peace While Staying Ready for War: The Challenges of U.S. Military Participation in Peace Operations (Paper), December 1999.

Structuring the Active and Reserve Army for the 21st Century (Study), December 1997.

The Army National Guard has eight combat divisions. In 1995, the official Commission on Roles and Missions reported that several of those divisions were not needed to carry out the nation's military strategy of being able to fight two nearly simultaneous major theater wars. Overall, the commission said, the Army has more than 100,000 excess combat troops that are not required for that security strategy. The commission also argued that the Guard has too many combat divisions even given its other missions, such as providing forces for rotation during wartime and supporting civil authorities at the state level.

This option would eliminate two National Guard combat divisions: one armored division and one mechanized infantry division. Doing so would reduce the Army's excess combat forces by about 35,000. The Army is planning to convert about 48,000 Guard combat troops into combat-support and combat-service-support troops (through the Army National Guard Division Redesign program), but that conversion would still leave the Army with more than 50,000 extra combat troops. This option would eliminate most of that excess. (Since the Army has identified a shortage of support forces, this option would retain all of the support personnel associated with the eliminated divisions.)

The primary advantage of this option is the savings it would generate. Cutting the two divisions would save the Army an average of about $550 million a year in operating costs over 10 years—funds that could be used to modernize the rest of the Army's active-duty and reserve forces more quickly. Eliminating those divisions could also help the Army avoid some future costs, since the equipment in the two disbanded divisions would not need to be modernized.

This option would have several disadvantages, however. First, it would reduce the number of reserve forces available as reinforcements during wartime. But how risky such a reduction would be is unclear, because analysts disagree about whether Guard combat forces could be ready to fight in time to help in a major theater war. Second, these cuts might reduce the Army's flexibility by leaving fewer reserve forces to use in peacetime missions. The Army has sent reserve combat troops to peace operations such as the long-running one in the Sinai Peninsula, and it plans to send more reservists to similar operations in the future. Third, this option would reduce the number of forces available for governors to call on to support missions in the states.

050-05 Cancel the Army's Comanche Helicopter Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	42	71
2002	165	183
2003	178	232
2004	277	296
2005	247	278
2001-2005	909	1,060
2001-2010	6,270	4,531

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATION:

An Analysis of U.S. Army Helicopter Programs (Study), December 1995.

Many of the Army's helicopters are beyond the end of their useful service life. Initially, the Army had planned to replace some of those older scout, attack, and utility helicopters with more than 5,000 new Comanche (RAH-66) helicopters. Comanche has had a troubled development program, however. The utility version of the helicopter was dropped in 1988 because the program had become too costly. In 1990, the size of the planned purchase was reduced from more than 2,000 aircraft to just under 1,300. Later, the Army delayed the projected start of Comanche production from 1996 to 2005.

Those changes have caused the procurement cost per helicopter to nearly double since the program began—from $11.7 million (in 2000 dollars) in 1985 to $21.5 million, based on current Army estimates. With that cost growth, Comanche is now more expensive than the Army's Apache (AH-64) attack helicopter, even though it was developed to be less costly to buy, operate, and maintain than other attack helicopters. Moreover, the General Accounting Office (GAO) and the Department of Defense's Inspector General (DoD IG) have stated that costs could grow by as much as another 30 percent. In addition, GAO recently reported that there are significant risks that Comanche will enter service later than expected and will not work as well as planned.

The primary advantage of Comanche over existing aircraft is its sophisticated stealth, avionics, and aeronautics technologies. However, some analysts would argue that the helicopter, which was conceived at the height of the Cold War, will no longer face threats of the same scale or sophistication as those for which it was designed. According to the DoD IG, the Army has not reexamined the mission requirements for Comanche in any depth since the end of the Cold War (although it will need to do so in the context of the Army Chief of Staff's new restructuring plan). Comanche is intended both to serve as a scout for Apache and to fill the scout and light attack role independently. But whether Comanche really does have a unique role to play in Army aviation is unclear. The Army is planning to use Apaches in both scout and attack roles for the next 15 to 20 years, as it did successfully during the Persian Gulf War. The Army also used armed scout helicopters, known as Kiowa Warriors, in the Persian Gulf both as scouts for Apache and as light attack aircraft. Moreover, the Army could use unmanned aerial vehicles (UAVs) for some scout functions. Secretary of Defense William Cohen testified that U.S. forces used UAVs as scouts in Kosovo effectively and without the risk of losing aircrews.

This option would cancel the Comanche program. The Army has already purchased enough Apaches to fill the attack role assigned to 13 of its 18 divisions, but it does need to replace the aging Cobras assigned to the attack aviation units of the remaining divisions. This alternative would buy 519 Kiowa Warriors by the end of 2010 to replace the Cobras still in service. Net savings would total about $6.3 billion over the 2001-2010 period. Some of the savings could be used to fund a program to continue development of advanced helicopter technologies. Abandoning the Comanche program, however, would mean that the Army would have to rely on helicopters designed in the 1960s and 1970s for years to come.

050-06 Cancel the Army's Crusader Artillery Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	201	117
2002	365	245
2003	280	225
2004	602	352
2005	569	419
2001-2005	2,016	1,358
2001-2010	6,687	5,444

SPENDING CATEGORY:

Discretionary

The Army plans to invest $13.7 billion (in 2000 dollars) to develop and procure more than 1,100 Crusader artillery systems. It considers the Crusader—which includes a self-propelled howitzer and a resupply vehicle—to be technologically advanced and significantly more effective than the service's current artillery systems.

Supporters cite several reasons why Crusader is needed. The Paladin, the Army's most modern artillery system, is too slow to keep up with other combat vehicles when armored forces advance. Its range is shorter than that of several foreign systems available to potential adversaries. And Paladin's peak firing rate of four rounds per minute is significantly slower than the 10 to 12 rounds per minute that the Army says it needs. Crusader's current design includes an automated resupply system, which makes a higher firing rate possible and reduces the crew size to six from Paladin's nine. Crusader is also designed with more sophisticated automation and better crew protection.

Opponents, however, question whether a heavy system such as Crusader has a role in the lighter, more mobile force envisioned for the future Army. Some also question how much improvement Crusader will actually deliver. It may be only 9 kilometers per hour faster than Paladin, and it has encountered technical difficulties. The original concept called for a gun using liquid propellant. The Army had to abandon that technology in 1996 because of technical and schedule problems. In addition, some Crusader subsystems embody technological innovations that have not yet been proved, and some have no backups in case of failure. For example, if the automatic munition reloader fails, Crusader will not be able to fire since it cannot be loaded manually. Those technical risks could prevent Crusader from meeting some of the Army's key requirements, in which case it might be no more effective than current systems. As part of a restructuring plan proposed by the Army Chief of Staff, General Eric Shinseki, the Army is now scaling back its requirements for Crusader to reduce the system's weight and is cutting the number of systems it will buy by more than 50 percent.

This option would cancel the Crusader program and provide funds to procure 550 German PzH 2000 self-propelled howitzers (with resupply vehicles), which the General Accounting Office has identified as a viable alternative to Crusader. The PzH 2000 fires eight to 10 rounds per minute, and its cross-country speed of 45 kilometers per hour is within the range required for Crusader. Purchasing that system could hedge against potential threats while freeing $6.7 billion over 10 years for the Army to pursue other promising technologies. For fire support in fast-moving advances, the Army could rely on the PzH 2000 systems or on the multiple-launch rocket system, which it used successfully in that role during the Persian Gulf War.

050-07 Cancel the Army's Tank Upgrade Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	525	85
2002	366	295
2003	377	379
2004	323	357
2005	123	307
2001-2005	1,712	1,422
2001-2010	2,107	2,064

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATION:

Alternatives for the U.S. Tank Industrial Base (Paper), February 1993.

The downsizing of the U.S. military and the unprecedented peacetime investment in modern weapons that occurred in the 1980s have sharply reduced the need for new weapons. In particular, the Army now has enough of the latest type of tank, the Abrams, to equip the forces it plans to field for the foreseeable future. As a result, the Army does not intend to buy new tanks for at least the next 15 years.

Instead, the Army has proposed upgrading about 1,000 M1s (the first model of the Abrams) to a later configuration, designated the M1A2. The upgrade program, which began in 1991 and ends in 2003, has two major goals: to increase the capability of Army tanks and to keep the facilities that produce tanks in business pending the need for a new tank to replace the Abrams. (Most of those facilities are owned by the government and operated by private contractors.)

In late 1999, the Army Chief of Staff presented a new vision for a much lighter and more rapidly deployable Army. One of its goals is a force that can deploy a brigade in four days, a division in five days, and five divisions in 30 days. Another goal is a force that can deploy abroad C-130 transport aircraft. What role heavy, current-generation tanks have in such a force is unclear. Upgrading those tanks might not be the best use of scarce funds. Also, although the M1A2 is 20 percent more capable than the M1 (as measured by one scoring system developed for the Department of Defense), converting 1,000 M1s to M1A2s would increase the total capability of the Army's 7,880 Abrams tanks by only 3 percent. That slight increase in capability would come at a high price—a total of about $3 billion over the next 10 years.

This option would cancel the Army's upgrade program but would keep some of the major components of the tank industrial base in a mothballed status. By preserving production facilities, the United States would retain the capability to make new or existing types of tanks in the future. Mothballing the government-owned facilities would require an initial investment. But after taking those costs into account, this option would save $525 million in 2001 and a total of $2.1 billion through 2010. Those funds could be used to develop new, lighter vehicles for the future Army.

Closing the tank production line would have some disadvantages, however. Without an upgrade program, the U.S. inventory would include fewer of the most capable M1A2 tanks. As regional powers acquired better tanks, the absence of M1A2s might erode the United States' advantage in a war, even though the M1A1 remains a highly capable tank. Perhaps the most important drawback of this option is that some companies that manufacture tank components might close and thus be unavailable to produce tanks in the event of a crisis. A related concern is the potential loss of workers whose skills are unique to tank manufacturing.

050-08 Reduce Procurement of the Virginia Class New Attack Submarine

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	0	0
2003	0	0
2004	400	30
2005	440	-60
2001-2005	840	-30
2001-2010	12,970	5,270

SPENDING CATEGORY:

Discretionary

As a result of the Quadrennial Defense Review, the Navy is reducing its force of attack submarines from 80 in 1996 to 50 by 2003. To meet that ambitious schedule, the Navy is decommissioning some of its Los Angeles class (SSN-688) submarines before they reach the end of their 30-year service life. (A recently released study prepared for the Chairman of the Joint Chiefs of Staff, however, calls for a force of 55 to 68 submarines. An option that examines increasing the attack submarine force to 68 appears in Congressional Budget Office, *Budget Options for National Defense*, March 2000.) Even as it is discarding older subs, though, the Navy is building newer ones. It ordered three Seawolf class submarines in the late 1980s and 1990s and is procuring the Virginia class New Attack Submarine (NSSN) to be their lower-cost successor. The reason for the additions is that the Joint Chiefs of Staff believe that the Navy will need 10 to 12 very quiet submarines by 2012 to compete with Russia's newest subs, which have become quieter, making them harder to locate and track.

The Virginia class submarine is designed to be as quiet as the Seawolf but will be smaller and slower, carry fewer weapons, and not be able to dive as deep. Although the Seawolf was designed primarily to counter the more severe threat posed by Russian submarines in the open ocean, the Virginia is being developed to operate in coastal waters close to potential regional foes.

The Navy ordered the first Virginia class submarine in 1998. It plans to buy one Virginia per year from 2001 to 2005 and two or three subs per year thereafter. Under that plan, 15 Virginia class submarines would be authorized between 2001 and 2010.

This option would save money by keeping the Los Angeles class submarines in service until the end of their normal 30-year life and slowing procurement of the Virginia class. To help maintain the industrial base for building subs and to modernize the fleet, the option would produce one Virginia per year from 2001 to 2010. At that pace, 10 Virginia class subs would be authorized between 2001 and 2010.

Producing the Virginia at low annual rates would save a total of almost $13 billion over the next 10 years. Most of those savings would occur after 2005, when the submarines would be produced at a lower rate. (Had CBO reflected a higher force goal in this option, savings would be lower.)

During the Congressional debate on producing the third Seawolf, the Navy emphasized that although Russia's economic troubles mean it cannot operate its nuclear submarine fleet up to potential, it is still buying new, very quiet attack submarines at low rates. The Seawolf and the Virginia would both be quiet enough to meet the Joint Chiefs' goal of competing with those new Russian subs. Procuring a total of 10 Virginias in addition to the three Seawolfs would enable the Navy to field a force of 13 very quiet submarines by 2012, meeting the Joint Chiefs' requirement.

050-09 Reduce the Number of Aircraft Carriers to Ten and Air Wings to Nine

	Savings (Millions of dollars) Budget Authority	Outlays
2001	4,460	850
2002	1,610	1,930
2003	1,940	2,320
2004	2,880	2,360
2005	1,740	2,410
2001-2005	12,630	9,870
2001-2010	24,370	22,660

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

050-10

RELATED CBO PUBLICATION:

Improving the Efficiency of Forward Presence by Aircraft Carriers (Paper), August 1996.

The aircraft carrier is the centerpiece of the U.S. Navy. The Administration's defense plans call for a fleet of 12 carriers—11 active ships plus one, manned partly by reserves, that can also be used for training. Those ships require a total of 10 active and one reserve air wings. (The number of active air wings is one less than the number of active carriers because one of the Navy's carriers is usually undergoing a major overhaul.) They will also be accompanied by a mix of surface combat ships (usually cruisers and destroyers) and submarines to defend against aircraft, ships, and subs that threaten the carriers. The surface combatants and submarines can also attack targets on land.

Since the Cold War ended, some policymakers have argued that the United States does not need a force of 12 carriers. The total capability of U.S. tactical aircraft in the Navy and Air Force will substantially exceed that of any regional power that seems potentially hostile. Moreover, the capabilities of U.S. ships are unsurpassed worldwide.

This option would immediately retire one conventionally powered aircraft carrier and one nuclear-powered carrier. By the end of 2001, the Navy would have 10 carriers (nine active ships and one partial reserve carrier for training purposes). In addition, this option would eliminate two active air wings, leaving eight active and one reserve wings.

Compared with the Administration's planned forces, those cuts could save $4.5 billion in 2001 and $24 billion over the next 10 years. Of that amount, $9 billion would result from not buying new carriers in 2001 and 2006, as now planned. The remaining savings would come from reduced operating costs associated with retiring two carriers and air wings. Those estimates include the cost of decommissioning the retiring ships—roughly $100 million apiece. (Cutting carriers could also reduce the number of surface combatants, submarines, and aircraft the Navy would need to accompany them. Thus, the Navy might save more money on procurement and operations by not having to buy and operate as many other new ships and aircraft. Conversely, the Navy might need those ships to perform other missions, such as forward presence, once it had fewer carriers.)

Although reducing the force to 10 carriers might not impair the United States' ability to fight and win two regional wars (according to one analysis by the Department of Defense), having fewer ships would limit the Navy's ability to keep three carriers deployed overseas most of the time. That could substantially increase the strain put on the carrier force as long as policymakers continued to use aircraft carriers to respond to crises or to provide U.S. presence overseas as extensively as they have in recent years. With fewer ships available, the time that those ships spent at sea could increase. The high-quality sailors the Navy needs would therefore spend more time away from their homes and families, perhaps making them less inclined to stay in the service. (An option that would increase the carrier fleet to 14 appears in Congressional Budget Office, *Budget Options for National Defense*, March 2000.)

The Navy might be able to maintain more overseas presence with carriers by bringing new crews to the ships while they were at their foreign posts rather than waiting for them to return home. (The Navy does that with some minesweepers.) In addition, the Navy could use ships other than carriers (such as large flat-deck amphibious vessels or Aegis cruisers) to help maintain U.S. presence overseas.

050-10 Use Marine Corps Squadrons to Fill Out Navy Air Wings

	Savings (Millions of dollars) Budget Authority	Outlays
2001	129	103
2002	265	229
2003	273	259
2004	280	274
2005	516	320
2001-2005	1,463	1,186
2001-2010	15,500	11,522

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-09, 050-12, 050-13-A, 050-13-B, and 050-14

RELATED CBO PUBLICATION:

A Look at Tomorrow's Tactical Air Forces (Study), January 1997.

The F/A-18 is the workhorse of both Navy and Marine Corps fighter fleets. It has operated from the decks of aircraft carriers and in Marine air wings since the early 1980s. The Navy has a requirement for 34 squadrons of F/A-18s for its carrier air wings. (Each squadron consists of 12 planes.) The Marine Corps has 18 squadrons of F/A-18s to provide air support to Marine ground forces.

To decrease what some critics see as unnecessary redundancy between the Marine Corps and Navy forces, this option would cut six of the Navy's F/A-18 squadrons—the planes in two operational carrier air wings—and use six Marine Corps F/A-18 squadrons in their place. That change would result in operating savings of about $300 million per year and a total of $2.8 billion through 2010.

Investment savings would also result because the Navy could decrease its purchases of the F/A-18E/F by about 185 planes (taking into account the aircraft in the six eliminated squadrons, as well as the additional planes that the military would have needed to buy for maintenance and training purposes and to make up for expected attrition.) Assuming those planes were eliminated from the end of the F/A-18E/F procurement program, savings in procurement would amount to $228 million in 2005 and $12.7 billion over 10 years. Savings from fighter-procurement funds could be especially helpful to the Department of Defense (DoD) since its planned spending on fighters may exceed the amount it will actually be able to devote to such purchases.

DoD may not need all of the F/A-18 squadrons in the Navy and Marine Corps for the type of conflict that is probable today. In the Cold War era, Navy, Air Force, and Marine Corps fighters would have been likely to operate in different areas during a major European war. Each of the Navy's operational carriers would have needed its full complement of aircraft to provide air support for itself and its accompanying ships. Those carriers might well have been assigned to other missions that would take them away from the flanks of NATO, where Marine Corps ground operations were likely to have taken place. Air Force fighters would have been engaged in combat with fighters of the former Soviet Union over central Europe. Thus, the Marine Corps would have had to rely on its own squadrons for air support. But today, critics say, even major theater wars will probably be sufficiently confined that aircraft carriers and their air wings will be able to remain in the theater to provide air support. Air Force fighters might also be on hand to give air support to Marine forces.

When operating in the same area, however, those various fighters face a problem of space. Because Marine Corps F/A-18 squadrons cannot operate from the shorter decks of the amphibious ships that transport marines and their equipment, those squadrons must use aircraft carriers while at sea. But they cannot operate from carriers that have a full complement of Navy aircraft, because the number of planes associated with today's notional carrier wings approaches the number that can actually operate from a carrier deck. Thus, in wartime, either the Marine Corps's or the Navy's fighter squadrons—but not both—could operate from the carriers' decks. In the face of equipment shortages, the Navy is already using five Marine Corps squadrons to fill out its carrier wings.

This option assumes that Marine Corps squadrons are kept rather than Navy squadrons. Marine Corps officers argue that the emphasis on both air and ground operations in their training makes them better suited to provide support to Marine ground units than pilots in Navy squadrons are. Moreover, Marine Corps pilots already train for such operations.

This option would have some significant drawbacks, however. It would cut a part of DoD's tactical air force structure that may be among the most useful in the future. Tactical aircraft have made significant contributions in recent conflicts. Fighter and attack aircraft have also been heavily used in recent peacetime operations, so cutting their number could further strain personnel and equipment in the units that remained. But an option such as this one may represent a force cut that will take place anyway, if future Administrations and Congresses are unable to devote more funds to fighter purchases.

050-11 Defer Purchases of the Marine Corps's V-22 Aircraft

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	0	0
2003	0	0
2004	22	3
2005	637	110
2001-2005	658	113
2001-2010	3,270	2,285

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

050-14

RELATED CBO PUBLICATION:

Moving the Marine Corps by Sea in the 1990s (Study), October 1989.

The V-22 aircraft, which entered production in 1997, is designed to help the Marine Corps perform its amphibious assault mission (seizing a beachhead in hostile territory) and its subsequent operations ashore. The plane's tilt-rotor technology enables it to take off and land vertically like a helicopter and, by tilting its rotor assemblies into a horizontal position, to become a propeller-driven airplane when in forward flight. As a result, the V-22 will be able to fly faster than conventional helicopters. The Marine Corps argues that the plane's increased speed and other design features will make it less vulnerable when flying over enemy terrain and will provide over-the-horizon amphibious assault capability.

Despite all of those advantages, the Bush Administration tried to cancel the V-22, largely because of its price tag. Each aircraft bought for the Marine Corps is expected to have a unit procurement cost of $61 million, on average—considerably more than most conventional helicopters. Nevertheless, the Congress has continued to fund the V-22, and the Marine Corps plans to buy a total of 360 planes. (The Air Force may eventually buy 50 V-22s for its special-operations forces, and the Navy plans to buy 48 for combat search-and-rescue missions and for logistics support of its fleet.)

The Marine Corps expects to acquire several other planes at the same time. During many of the years that it is purchasing V-22s, it also plans to buy large numbers of Joint Strike Fighters (JSFs) to replace its short-range bomber, the AV-8B, and its F/A-18 fighter attack aircraft. JSFs are expected to be relatively inexpensive as tactical fighters go—perhaps 60 percent of the price of the Air Force's sophisticated F-22. But when bought in quantity and combined with the cost of the V-22, their purchase would bring peak annual spending on the V-22 and JSF to about $5.5 billion—roughly five times the amount requested for Marine Corps combat aircraft in this year's budget. (Technically, the V-22 and JSF are bought with Navy procurement funds.) If the Marine Corps cannot increase funding for those aircraft, it may have to modernize either its fighter fleet, its airborne amphibious assault fleet, or both more slowly.

This option would halve the Marine Corps's annual procurement of V-22s during the 2005-2010 period, when both V-22s and JSFs would be bought. As a result, the service's average funding requirements during those years would decrease to about $5 billion. That sum may be more manageable than the Marine Corps's current plan and would save almost $3.3 billion over 10 years.

Deferring purchases of V-22s would have drawbacks, however. The current amphibious assault fleet is made up of CH-46 and CH-53 helicopters that are more than 30 years old, on average. The CH-46s would remain in the fleet until their average age approached 50 if the V-22s deferred under this option were bought beginning in 2013, when planned V-22 purchases decrease sharply. (If the Marines had to engage in an extensive modification effort to retain those helicopters longer, the savings shown at left would be lower.) Also, the amphibious assault fleet provides more unique services than the Corps's fighter attack fleet. The Marines can probably count on the Navy's carrier-based F/A-18 aircraft to provide them with additional firepower, but they cannot get aerial amphibious assault assets anywhere else. Also, cutting V-22 purchases might decrease the Corps's ability to perform humanitarian missions and other peacekeeping activities, which have grown more common in recent years.

050-12 Reduce Air Force Tactical Forces

	Savings (Millions of dollars) Budget Authority	Outlays
2001	307	245
2002	632	550
2003	650	623
2004	669	654
2005	688	678
2001-2005	2,945	2,750
2001-2010	6,679	6,438

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

050-13-A, 050-13-B, and 050-14

RELATED CBO PUBLICATION:

A Look at Tomorrow's Tactical Air Forces (Study), January 1997.

Today's Air Force includes about 20 tactical air wings—13 on active duty and seven in the reserves. (An Air Force tactical air wing traditionally consists of 72 combat planes, plus another 28 for training and maintenance purposes.) Substantial disagreement exists about whether all of those air wings are necessary, since U.S. tactical aircraft enjoy overwhelming superiority compared with the forces of any regional power that appears potentially hostile to the United States.

This option would reduce the Air Force's tactical fighter forces to 18 air wings by the end of 2001. That pace of reductions might be feasible inasmuch as the Air Force has cut the size of its fleet quickly in the past: it eliminated six air wings between 1990 and 1992 and another six by the end of 1996. Reducing the number of Air Force wings from 20 to 18 would lower the service's operating costs by $307 million in 2001 and $6.7 billion through 2010.

Further savings might be possible if the Air Force accompanied the force reduction with a reorganization that increased the number of planes per squadron and eliminated more squadrons. That practice (known as "robusting") allocates resources more efficiently, since each squadron or wing has high fixed costs. Increasing all Air Force squadrons to 24 planes could add significantly to the savings shown at left, though only if the Department of Defense (DoD) restructured units and bases to reduce overhead costs.

A reduction to 18 Air Force wings might leave the United States with an acceptable number of capable fighters. Even in terms of simple numbers, U.S. fighter inventories exceed those of any potential regional aggressor. Also, U.S. aircraft are more sophisticated than those of potential enemies.

However, retaining only 18 wings in the Air Force would not meet the military's current estimate of its requirements. Today's force planning assumes that the United States needs to be able to fight virtually simultaneous wars in two regions of the world—one in the Middle East and another, perhaps, in Asia. Winning two nearly simultaneous regional conflicts would require a minimum of 20 air wings, DoD has suggested.

Some analysts would also argue that additional cuts in Air Force wings ignore a major lesson from the Persian Gulf War: that aerial bombardment by tactical aircraft can be very effective and may greatly accelerate the end of a war, thus reducing loss of life among U.S. ground troops. The recent war in Kosovo was waged chiefly by U.S. and allied air forces, further emphasizing their key role in future conflicts. A sizable inventory of tactical aircraft—perhaps more than would be maintained under this option—might therefore be a wise investment.

050-13-A Reduce Purchases of the Air Force's F-22 Fighter

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	320	46
2003	1,735	378
2004	1,842	1,045
2005	1,906	1,541
2001-2005	5,803	3,010
2001-2010	22,223	16,242

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-11, 050-13-B, and 050-14

RELATED CBO PUBLICATION:

A Look at Tomorrow's Tactical Air Forces (Study), January 1997.

The F-22 is being developed as the Air Force's next premier fighter aircraft and is scheduled to begin replacing the F-15 soon. But the plane has experienced repeated delays, reductions in quantity, and increases in price during its almost 20-year development. This option would decrease the planned purchase of F-22s by 219 planes. Assuming that the reduction was evenly distributed over the F-22's purchase period, it would save a total of $22.2 billion through 2010, although the savings would not begin until 2002. (A related option, 050-13-B, would cancel production of the F-22 altogether.)

The Air Force originally planned to buy more than 800 F-22s. After a series of cuts, the latest plan will buy only 339 aircraft—enough for about three air wings. Even if the Air Force makes no further cuts to planned purchases, it will have to pay $120 million apiece for the F-22. That price will purchase a number of improvements in capability over other fighters. Even so, the F-22's cost makes it the most expensive fighter ever built.

The F-22 is the only tactical fighter program to survive from the Cold War period. (The other two fighters that the Department of Defense is planning—the Joint Strike Fighter and the Navy's F/A-18E/F—entered development after 1990. They are likely to be both less capable and less expensive than the F-22, although they may face many of the same threats.) The F-22's sophistication and cost, plus concerns about whether the plane will actually realize promised improvements in capability, have led some people to suggest that the F-22 is a legacy of the Cold War—a plane designed to fight many sophisticated Soviet fighters rather than the modest regional fighter forces it is more likely to encounter today. Such critics recommend canceling the program, or at least cutting planned procurement further. In its report on its fiscal year 2000 defense appropriation bill, the defense subcommittee of the House Committee on Appropriations expressed concerns about the plane’s cost and capability. The Senate concurred and the Congress directed DoD to complete testing of the F-22 before spending procurement funds on production.

The Air Force could reduce production quantities to a total of 120 F-22s, enough to let the service field one air wing of the sophisticated fighters. Such a "silver-bullet" purchase would allow the Air Force to learn lessons about producing aircraft of the F-22's technological complexity but might still leave more than enough planes to perform the missions for which the service needs the F-22's degree of stealth and other performance advantages.

One possible disadvantage of this option is that it would make the Air Force’s fighter fleets, which are already aging under current plans, even older. However, buying 219 F-15s to replace the cut in F-22s would remedy that problem. Although the F-15 is much less capable than the F-22, it is far more capable than the fighters of almost any of the United States’ regional adversaries. A one-for-one offset of F-15s for F-22s would lower the 10-year savings from this option to $10 billion.

050-13-B Cancel Production of the Air Force's F-22 Fighter

	Savings (Millions of dollars) Budget Authority	Outlays
2001	3,069	655
2002	3,952	2,080
2003	5,037	3,174
2004	4,799	3,969
2005	4,799	4,467
2001-2005	21,657	14,344
2001-2010	43,091	36,842

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-11, 050-13-A, and 050-14

RELATED CBO PUBLICATION:

A Look at Tomorrow's Tactical Air Forces (Study), January 1997.

As option 050-13-A discussed, although the Air Force has great hopes for its new F-22 fighter, the aircraft's development program has experienced numerous delays, reductions in quantity, and increases in price over almost 20 years. If the program does not deliver as promised—or if leaders in the Congress and the Department of Defense (DoD) decide that the plane's capabilities are too expensive to afford in today's budget environment—the F-22 could be canceled. Doing that without making any provisions for replacing the plane would save $3.1 billion in 2001 and a total of $43 billion over 10 years. If F-22 purchases were offset with F-15s, savings would drop to $2.4 billion in 2001 and $25 billion over 10 years.

Outright cancellation would save more money than a "silver-bullet" purchase of F-22s (as described in option 050-13-A). But it would have several disadvantages. Cancellation of the F-22 could affect development of the Joint Strike Fighter, since DoD expects the two planes to have common design elements. In addition, the U.S. military might need the F-22's stealthy design and other characteristics if other countries improved their fighter capabilities. Finally, if beginning another top-of-the-line fighter program to replace the F-22 proves necessary, some of the costs already incurred in developing the F-22 could be paid again in a new development program, adding to the government's overall costs.

050-14 Slow the Schedule of the Joint Strike Fighter Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	687	407
2002	-73	183
2003	284	178
2004	557	398
2005	1,604	675
2001-2005	3,058	1,841
2001-2010	22,320	16,051

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-09, 050-11, 050-12, 050-13-A, and 050-13-B

RELATED CBO PUBLICATION:

A Look at Tomorrow's Tactical Air Forces (Study), January 1997.

One of the military's most ambitious aircraft development programs is the Joint Strike Fighter (JSF) program. Variants of the JSF are intended to replace planes in the Air Force, Navy, and Marine Corps; they account for two-thirds of the fighter aircraft the military expects to buy through 2020. The Department of Defense (DoD) intends to develop and begin purchasing the JSF by 2005—only nine years after the plane's first acquisition milestone. That interval is about 40 percent less than the time DoD has spent developing the F-22, the other new jet fighter it is developing from scratch. Many experts question whether DoD will actually be able to keep to such a tight schedule in a program that is supposed to produce three versions of the aircraft for three services.

This option would postpone fielding the JSF by two years to make the program's schedule more closely reflect recent experience with fighter development. That slowdown in development and production would decrease requirements for funding by $3 billion over the next five years and $22.3 billion through 2010.

The program office expects to need a total of about $23.4 billion to develop the three variants of the Joint Strike Fighter: an inexpensive multirole fighter for the Air Force; a longer-range, stealthy, ground-attack plane for the Navy; and a short-takeoff/vertical-landing fighter for the Marine Corps. (That sum includes about $1.3 billion invested by several foreign governments, including the United Kingdom's, that expect to purchase one or more of the variants.) The JSF program amalgamated three fighter programs that had been under way: the Air Force's multirole fighter, the Navy's A/FX, and the Marine Corps's ASTOVL program. Although the JSF variants will perform significantly different missions, they are expected to have much in common. DoD wants them to be more capable than current-generation aircraft but only slightly more expensive, if at all.

Satisfying the diverse needs of prospective users of the JSF could be challenging. Nevertheless, DoD plans to begin buying the planes just six years from now. The Joint Strike Fighter became a major defense acquisition program in May 1996; under the current schedule, the first formal review will take place in 2001, when the program is scheduled to enter the engineering and manufacturing stage of development (EMD). The JSF would then be produced in 2005, just four years after EMD began and nine years after it became a major acquisition program. The F-22 program, by contrast, has already been running for 14 years and may take a year or more to enter low-rate production (see options 050-13-A and 050-13-B). Some analysts might argue that the F-22's experience is not a good indicator for the JSF, since the F-22 was expected to represent a greater technological leap over its predecessor. But with the JSF's multiple missions and sponsors and the services' ambitious cost goals for the fighter, others might argue that the JSF program will be even more complex.

If the original JSF schedule is actually attainable, delaying it by two years would have several major drawbacks. Despite saving money in the near term, the delay could add to development costs. In addition, delay would exacerbate the aging problem of DoD's fighter fleets. Even under current plans for the JSF, when large-scale deliveries begin toward the end of the next decade, fighters in the Navy and Marine Corps fleets will be an average of almost 15 years old. The Air Force fighter fleet will average almost 20 years of age when that service receives bulk deliveries of JSFs. Both averages exceed the ages at which each of those services has retired fighter planes in the past.

If, however, delays in developing the JSF are inevitable, a less ambitious, more realistic schedule would add to neither costs nor fleet ages. Revising the JSF schedule would permit DoD to plan its future courses of action better. For example, actions to deal with fleet aging might include buying more current-generation aircraft or modifying the planes in existing fleets.

050-15 Create Common NATO Airlift and Cut U.S. C-17 Costs

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	1,893	274
2003	943	890
2004	80	981
2005	179	637
2001-2005	3,094	2,783
2001-2010	4,037	3,983

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATIONS:

Moving U.S. Forces: Options for Strategic Mobility (Study), February 1997.

Assessing Future Trends in the Defense Burdens of Western Nations (Paper), April 1993.

The C-17 Globemaster III is a four-engine transport aircraft that can carry at least 110,000 pounds of cargo for 3,200 nautical miles without aerial refueling. Because it is designed to land at small airfields with short runways, the C-17 could help meet transport needs within a theater of combat as well as over long distances. The current plan for transporting U.S. forces to regional conflicts calls for a fleet of 120 C-17s. At the same time, seven of the United States' European allies in the North Atlantic Treaty Organization (NATO) are planning to buy a total of 289 transport aircraft to carry reaction forces to crisis spots outside the territory of NATO members, in accordance with NATO's Strategic Concept.

This option would create a common NATO airlift fleet of 20 C-17s (similar to the common NATO AWACS fleet based in Germany, for which the United States pays 41.5 percent of operating and modernization costs). Twenty C-17s that the Air Force plans to buy in 2002 and 2003 would be transferred to NATO, which would reimburse the Air Force for them by the beginning of each year in order to comply with full-funding requirements. The average cost of those planes is about $200 million apiece.

A common NATO airlift fleet would enable the allies to deploy forces to a crisis zone, while allowing the United States to draw on those assets for non-NATO missions under the Combined Joint Task Force (CJTF) concept approved in 1996. That concept allows NATO members—with consensus from the alliance—to use NATO assets for missions other than defense of a member state.

Assuming that the United States paid 41.5 percent of the cost of the NATO airlift fleet, this option would achieve net savings for the United States of $3.1 billion over five years and $4.0 billion over 10 years, including net savings of about $200 million per year in operation and support costs once all 20 aircraft were delivered. It also would give the European allies faster access to strategic airlift than would otherwise be the case.

This option would face two main obstacles, however. The first is the European countries' desire to protect their defense industries by building their own strategic transport plane. The seven countries involved have committed to a joint program to develop the Future Large Aircraft (FLA), to be produced by the Airbus consortium. That plane would carry less cargo than the C-17 and be cheaper (at $75 million apiece). Alternatively, the Europeans could consider buying Airbus commercial aircraft, although such planes are more difficult to load and unload, cannot carry very large cargo, and cannot land on some shorter or unpaved runways. Enthusiasm for developing the FLA is waning, however. In an indication that they will consider alternatives, Britain, France, Spain, and Belgium have all solicited bids from U.S. firms for a total of 143 aircraft, and Britain intends to lease four C-17s or their equivalent.

The second obstacle involves the political ramifications of relying on NATO to provide part of the U.S. Air Force's lift capability. The CJTF concept, designed to let European coalitions act without U.S. involvement, is new and evolving. Conceivably, if a NATO member opposed a mission (such as France opposing military action against Iraq), it might be able to veto U.S. use of NATO assets. Some Members of Congress might find that saving money would not outweigh the risk of diminishing the U.S. ability to act unilaterally if necessary.

050-16 Cut Requirements for Pilots in Nonflying Positions

	Savings (Millions of dollars) Budget Authority	Outlays
2001	145	115
2002	204	184
2003	238	224
2004	272	259
2005	306	294
2001-2005	1,164	1,077
2001-2010	2,862	2,754

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATION:

Statement of Christopher Jehn, Assistant Director, National Security Division, on Pilot Retention: Issues and Possible Solutions, before the Subcommittee on Military Personnel of the House Committee on Armed Services (Testimony), March 4, 1999.

The Air Force and the Navy have fewer pilots than their stated requirements call for. In 1999, both services reported shortfalls of more than 1,000 pilots. The two services have undertaken several initiatives to address that problem, including paying special bonuses under the Aviation Continuation Pay program. But despite those efforts, pilot shortfalls are expected to persist for the foreseeable future.

This option would use an additional approach to address that problem: reducing the stated requirements for pilots in nonflying positions. Cutting those requirements by two-thirds would save $115 million in outlays in 2001 and $2.7 billion over 10 years by reducing the number of pilots who would need to be trained.

Both the Air Force and the Navy have many more pilots than they need for critical cockpit or flying positions. The shortfalls reflect the fact that the services have included many nonflying positions in their requirements for pilots. At the end of 1998, for example, nearly one-fourth of the Air Force's roughly 13,400 pilots were in nonflying positions, as were about half of the Navy's 6,600 pilots.

Supporters of this option would argue that some of the nonflying billets identified as requiring pilots are already being adequately filled by personnel with other backgrounds. In addition, the services could employ aviation navigators in some nonflying positions that require the expertise of a pilot.

The principal disadvantage of this option is that reducing the number of nonflying positions reserved for pilots could limit pilots' opportunity to gain the broader experience they need to progress in their careers. That problem might be alleviated, however, if the Air Force and Navy established a fly-only career path specifically for pilots who wanted to spend all 20 years of their military service in flying assignments. (Some pilots have indicated that they joined the military to fly and might be willing to stay in such a career path even if it limited their ability to be promoted.) A fly-only career path would lessen the number of nonflying positions needed to provide pilots with career-broadening opportunities. Another disadvantage of this option is that it might not leave enough shore billets for Navy pilots to rotate into between their tours at sea.

050-17 Restructure the Officer Corps

	Savings (Millions of dollars) Budget Authority	Outlays
2001	-242	35
2002	123	331
2003	517	655
2004	904	982
2005	1,644	1,394
2001-2005	2,945	3,397
2001-2010	12,120	11,990

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATION:

The Drawdown of the Military Officer Corps (Paper), November 1999.

As part of the post-Cold War drawdown in the military, each of the services cut its officer corps significantly. Those cuts, however, were accompanied by a change in the composition of the armed forces. The ratio of enlisted personnel to officers declined from 6.0 to 1 in 1989 to 5.2 to 1 in 1999 because the officer corps was cut by a smaller percentage than enlisted personnel. The percentage of senior officers—those in the general or flag grades as well as the so-called field grades (major through colonel)—increased. The percentage of officers who entered the military through the service academies also rose.

This option would offset those apparent consequences of the drawdown. It would return the enlisted-to-officer ratio and the percentage of general and flag-level officers to the levels that existed in 1989, when the drawdown began. In addition, the percentage of newly commissioned officers trained in the service academies would be reduced. The option would also reduce the number of field-grade officers, restoring the limits on those positions to levels consistent with the Defense Officer Personnel Management Act before the drawdown. Compared with the Administration's budget request for 2000, those changes would save $35 million in outlays in 2001 and a total of $12 billion through 2010.

In carrying out the drawdown, the services tried to protect officers who were already in the force, many of whom had based their career expectations and financial plans on continued military service. The decline in the enlisted-to-officer ratio suggests that those efforts may have created an unbalanced force. The services might argue that the decline was driven by changing requirements as a result of new technologies and military doctrines that have decreased the need for enlisted personnel relative to the need for officers. But some critics see the timing of the shift as suspicious. Moreover, when the drawdown began, none of the services expected that their future requirements for enlisted personnel would fall as much as they did relative to requirements for officers. This option would restore the enlisted-to-officer ratio to the 1989 level of 6.0 to 1 by reducing the size of the officer corps by about 15,900 and increasing the size of the enlisted force by an equal amount.

That reduction would be targeted primarily toward officers in the field, general, and flag grades. The percentage of general and flag officers would be reduced gradually to the 1989 level by restricting promotions into those grades. Reductions in the field grades could be achieved by encouraging officers to leave the service voluntarily, through such programs as the temporary early retirement authority (TERA), voluntary separation incentive (VSI), and special separation benefit (SSB).

Over a period of four to five years, the number of general or flag officers would be reduced by about 200 through attrition, while about 12,600 field-grade officers and 3,100 junior officers (second lieutenant through captain) would be separated. Assuming that field-grade officers with less than 20 years of service would receive TERA and those with 6 to 15 years of service would receive VSI or SSB, the savings in pay would initially be offset entirely by the cost of separation payments. Net savings in pay would amount to a total of $9.6 billion through 2010.

Supporters of this option would argue that the services' actions have resulted in a force that is too senior and contains more officers than needed to lead the remaining enlisted personnel. In their view, much of the expertise and combat readiness that senior officers provide could be obtained at lower cost from highly capable senior enlisted personnel and junior officers. Opponents, by contrast, might argue that separating additional senior officers would constitute a breach of faith because it would cut short the careers of some service members. Moreover, the services' efforts to implement the Goldwater-Nichols Defense Reorganization Act of 1986 and the Defense Acquisition Workforce Act of 1990 may have increased requirements for those relatively senior officers.

This option would also return the mix of academy and nonacademy graduates entering active duty to the level that prevailed before the drawdown. Although the number of students in the service academies declined during the drawdown, academy graduates account for 14 percent of new officers now compared with 9 percent in the early 1980s. Under this option, the total number of officer accessions would remain at the level planned by the Department of Defense, but the services would draw more officers from lower-cost commissioning programs—the Reserve Officer Training Corps (ROTC) and Officers Candidate School/Officer Training School (OCS/OTS)—and fewer from the more costly service academies. The estimated savings from that action reflect only the costs that would change in the near term, such as operating expenses and pay for faculty and cadets. Those savings would be partially offset by additional costs of about $350 million over 10 years to procure officers from OCS and ROTC to replace those from the academies. As a result, this change would save $75 million in outlays in 2001 and a total of nearly $2.4 billion through 2010. In the longer term, savings might also accrue from changes in the academies' physical plant.

Supporters of changing the mix of new officers might argue that the academies are larger than many successful private colleges and that additional cuts to them are feasible. Moreover, a balanced mix of academy graduates and accessions from other commissioning programs may be needed to maintain good civil/military relations and ensure that the officer corps reflects the full diversity of U.S. society. Opponents of that change would contend that the service academies are the best source of future military leaders and that academy graduates are well worth the dollars spent on them. Some opponents might also argue that the academies have already reduced their class size to the minimum efficient level.

050-18 Deny Unemployment Compensation to Service Members Who Leave Voluntarily

	Savings (Millions of dollars) Budget Authority	Outlays
2001	134	134
2002	145	145
2003	162	162
2004	181	181
2005	188	188
2001-2005	810	810
2001-2010	1,852	1,852

SPENDING CATEGORY:

Discretionary and Mandatory

Many military personnel who voluntarily leave active-duty service are eligible for unemployment benefits. That situation contrasts with the situation of civilian workers—who must have left their job involuntarily to qualify for unemployment compensation—even though payment amounts for the two groups are calculated the same way.

This option would subject former military personnel to the same rules as members of the civilian labor force; in other words, only personnel who left the service involuntarily would be eligible to receive unemployment benefits. That change would reduce the number of departing personnel eligible for benefits by at least two-thirds and save an average of $185 million annually through 2010. Because the Department of Defense ultimately reimburses the Department of Labor for the cost of unemployment payments to former service members, most of those savings ($1.8 billion through 2010) would occur in the defense budget. A small portion of the savings ($57 million through 2010) would occur in the Department of Labor's budget. (The latter savings would be in mandatory spending.)

Most personnel who leave military service do so voluntarily. Many choose not to reenlist after completing a term of service; others, who have served for a minimum of 20 years, opt for voluntary retirement. A much smaller group is separated involuntarily for reasons related to job or promotion performance or, in recent years, to the drawdown of military forces. Although the pressures associated with the drawdown may have blurred the line between voluntary and involuntary separation in the past, the end of the drawdown has restored that distinction.

Proponents of this option would argue that in addition to saving money, it would subject military personnel to the same rules as the rest of the workforce. Thus, in their view, it would make more equitable use of an entitlement program that was established with the intent of aiding people who lost their job involuntarily.

Critics, by contrast, might argue that the frequent moves associated with military service mean that members who separate voluntarily are unlikely to take up residence in the area of their final posting, making it difficult for them to find a new job before they leave the service. In those critics' view, voluntary separation from military service is not comparable with voluntary termination of civilian employment and therefore should not be subject to the same restrictions on eligibility for unemployment compensation.

050-19 Downsize the Military Medical System

	Savings (Millions of dollars) Budget Authority	Outlays
2001	-241	-408
2002	-700	-1,041
2003	222	-442
2004	1,284	736
2005	3,204	2,719
2001-2005	3,770	1,565
2001-2010	31,097	27,687

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

050-20

RELATED CBO PUBLICATION:

Restructuring Military Medical Care (Paper), July 1995.

The extensive medical system run by the Department of Defense (DoD) is the chief source of health care for some 5.3 million people in the United States. DoD's primary justification for the system is that it is necessary to ensure care for service members in wartime. During peacetime, the system trains medical personnel for war and provides care for active-duty service members, retirees, and dependents of both groups.

This option would substantially reduce the size of DoD's direct care system, cutting the number of beds in military facilities to the amount that DoD would need to care for two-thirds of the casualties it anticipates from two nearly simultaneous major wars. As part of that downsizing, DoD would convert many military hospitals into outpatient clinics, close other facilities, and reduce the number of active-duty physicians. This option would also discontinue the Tricare program for retirees and all types of dependents, requiring them to seek care in the civilian sector. Those younger than 65 would be offered coverage through the Federal Employees Health Benefits (FEHB) program, and those 65 or older (who now receive care at military hospitals and clinics only when space is available) would use their Medicare coverage and any private insurance they obtained.

Such restructuring of the military medical system would require additional spending in the near term but would offer substantial savings later on. Total net savings in outlays would be nearly $28 billion through 2010. That estimate reflects savings from operating a smaller military system, assuming that DoD faces the same upward pressures on the cost of care that private-sector providers and insurers do. It also takes into account higher Medicare spending (as older military beneficiaries rely more heavily on their Medicare benefits), the costs of closing facilities, and the costs of providing FEHB coverage to beneficiaries younger than 65. Under this option, DoD would pay the same share of the premiums for FEHB health plans that other federal agencies do for their civilian employees. In addition, families of active-duty service members who enrolled in FEHB would receive a voucher that covered much or all of the remaining share of the premium.

Supporters of downsizing note that although DoD's wartime medical requirements during the Cold War were based on the scenario of a large conventional conflict in Europe, more recent planning scenarios have led to sizable cuts in those requirements. Today, between military medical facilities, hospitals run by the Department of Veterans Affairs, and civilian facilities that have agreed to provide beds during a national emergency, the United States has more than twice the hospital capacity needed to meet the current wartime demand for 13,400 beds. Moreover, even after making the reductions in this option, DoD would still have about 9,000 beds in its expanded system—a much higher percentage of its wartime requirement than it met during the Cold War.

DoD would probably see several disadvantages, however, to making such deep cuts to its health care system. Military medical officials argue that DoD facilities and the care they provide in peacetime are essential for recruiting and training physicians and ensuring medical readiness. Downsizing that system to such an extent would require DoD to modify the way it trains and prepares for wartime. For example, it would need to strengthen ties with the civilian sector to provide casualty training for military medical personnel and to continue ensuring an adequate supply of beds for wartime.

Another potential drawback of this option is that those older beneficiaries who are able to rely on military facilities would have to seek care elsewhere. In addition, some beneficiaries who enrolled in FEHB plans would pay substantially more out of pocket than they do for care in the military system. Military retirees and their dependents would pay about 30 percent of their FEHB premium. (Dependents of active-duty members would pay little or no premium after receiving their voucher.) And enrollees in most FEHB plans would face copayments or deductibles for outpatient visits, prescription drugs, and other medical services.

Proponents of this option would counter that higher out-of-pocket costs could prompt more prudent use of medical care than in DoD's direct care system, where many services are provided at no or low cost. In addition, they might say, many FEHB plans would offer improved coverage and so might be worth the greater out-of-pocket expense. Moreover, the value of DoD's health benefits has grown dramatically with advances in technology and medical practices. Thus, proponents would argue, it is reasonable for military beneficiaries to share more of the costs associated with those advances—as many people covered by employer-sponsored plans in the private sector already do.

050-20 Revise Cost Sharing for Military Health Benefits

	Savings (Millions of dollars) Budget Authority	Outlays
2001	327	276
2002	437	411
2003	444	436
2004	455	451
2005	467	463
2001-2005	2,131	2,037
2001-2010	4,135	4,025

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

050-19

RELATED CBO PUBLICATION:

Restructuring Military Medical Care (Paper), July 1995.

Some 8.1 million active-duty service members, military retirees, and their dependents are eligible to use the military health care system worldwide, yet only 5.8 million actually do on a full-time basis. Because the Department of Defense (DoD) does not require users to enroll, many of them choose to seek military care on a case-by-case basis to augment other insurance coverage. Thus, military planners face major uncertainties about their patient load and health care costs each year.

The military health system offers three types of coverage: Tricare Prime, a plan similar to health maintenance organizations; Tricare Standard, a traditional fee-for-service insurance program; and Tricare Extra, a preferred provider option. Beneficiaries must enroll in Tricare Prime if they wish to use it, or they may use Tricare Standard or Extra without enrolling.

This option would make three changes to that system. First, all beneficiaries (except those on Medicare) would have to enroll in one of the three programs before using the military health care system. The annual enrollment fee for Tricare Prime would remain the same (no charge for active-duty personnel and their families and $230 for single coverage or $460 for family coverage for retirees). Under Tricare Extra or Standard, active-duty personnel would still pay no fee, but retirees would pay $115 a year for single or $230 for family coverage. Second, DoD would adjust enrollment fees for inflation by the annual change in the consumer price index for medical expenses. Third, users of Tricare Prime would pay the same copayments for outpatient care at military facilities (where they now pay nothing) as they do at civilian providers. In addition, all retirees would begin to pay small copayments if they chose to receive care at military facilities.

Together, those three changes would lower discretionary appropriations by $327 million in 2001 and $4.1 billion through 2010. The savings would stem from enrollment fees, increased copayment charges, and more prudent use of care by beneficiaries. Under current law, DoD is allowed to spend some of the revenues it collects through copayments. This estimate assumes that the Congress would reduce DoD's appropriations by the amount of revenue collected under the option. However, if the Congress revoked DoD's automatic reimbursement authority, the estimate would take the form of an offset to mandatory spending.

By requiring beneficiaries to enroll, DoD could identify who uses its system. Military providers need to plan for the health care needs of a defined population to develop per capita budgets and build cost-effective delivery networks.

Proponents of this option could argue that the value of DoD's health benefits has risen with advances in medical technology, so users should expect to bear some of the associated cost, just as employees of private firms have. In addition, charging copayments would help curb excessive use of services by creating the same incentives for beneficiaries who receive care on-base as for those who use civilian providers. It would also eliminate the inequity of providing more generous benefits to people who live near a military hospital or clinic.

On the negative side, many military families and retirees would view even modest copayments at military facilities as an erosion of their benefits. Retention and morale might suffer, even though this option would still offer service members and their families more generous health benefits than most government or private-sector employers do.

050-21 Have DoD and VA Purchase Drugs Jointly

	Savings (Millions of dollars) Budget Authority	Outlays
2001	26	21
2002	74	63
2003	78	74
2004	82	80
2005	86	84
2001-2005	346	323
2001-2010	843	810

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

700-05

In 1997, the Departments of Defense (DoD) and Veterans Affairs (VA) spent about $1 billion and $1.3 billion, respectively, on pharmaceutical products for patients in their health care systems. Nationwide, spending on prescription drugs has grown roughly twice as fast in recent years as total national health spending. Constraining such cost growth is an important goal for DoD and VA: each operates its large health care system on a fixed annual appropriation, so spending more on prescription drugs means it has fewer resources to devote to other types of care for its beneficiaries.

This option would consolidate DoD's and VA's purchases of pharmaceutical products, as the Congressional Commission on Servicemembers and Veterans Transition Assistance has recommended. Specifically, it would require the two agencies to organize a joint procurement office and develop a common clinically based formulary (a list of prescription drugs that both agencies' health plans would agree to provide). Formularies can save money by encouraging providers to substitute generic versions for brand-name drugs or by selecting one or more preferred brand-name drugs within a therapeutic class. The joint formulary would apply throughout the VA health system, to mail-order pharmacy services, and at military hospitals and clinics. Once in place, it would allow the agencies to enter into more "committed-volume" contracts with pharmaceutical manufacturers, which generally lead to lower drug prices. In addition, this option would merge the two agencies' mail-order pharmacy services. Those changes would save DoD and VA a total of $21 million in outlays in 2001 and $810 million through 2010.

In recent years, DoD and VA have made efforts to combine some purchases, but that collaboration is limited, and they continue to maintain separate formularies and procurement offices. The VA's National Acquisition Center (NAC) is responsible for purchasing prescription drugs for most federal agencies except DoD, and it negotiates and maintains the federal supply schedules of prices for those items. The Defense Supply Center Philadelphia (DSCP), an office of the Defense Logistics Agency, negotiates prices for pharmaceuticals and draws up contracts with vendors to buy and deliver those products to military treatment facilities. DSCP also makes plans to deliver those items overseas quickly in the event of a conflict.

Proponents of joint purchasing would argue that DoD and VA need to rein in the rapid growth of prescription drug costs. Without such measures, both agencies may be forced to ration more tightly the care they provide. In addition, those proponents would say, the need for separate procurement offices is not apparent. According to a 1998 report by DoD's Inspector General, only 0.05 percent of the items that the DSCP procures on behalf of military facilities are "militarily unique"; most are common items. VA officials maintain that the National Acquisition Center has already achieved significant savings on many of its pharmaceutical purchases through committed-volume contracts.

In developing a common formulary, the two agencies would need to adopt procedures by which physicians could prescribe nonformulary drugs to patients who needed them. (For example, a patient would require an alternative drug if he or she was allergic to the formulary drug in a therapeutic class.) The design and execution of such an exception process would affect the savings from this option. The stricter the process, the higher would be the cost of documenting and judging the patient's need for a nonformulary drug. A less restrictive process, however, would reduce the government's bargaining power and could reduce the savings from this option.

Critics of consolidation argue that such savings are unachievable anyway. The veterans who obtain health care from the VA make up a very different mix of medical cases than military beneficiaries do—for example, more of them suffer from mental illness, substance abuse, or severe disabilities (such as spinal cord injuries). Thus, the degree of overlap in prescription drugs dispensed by the two agencies may be limited.

Opponents of this option also argue that DoD and VA have already taken important steps to expand their joint procurement. They have entered into 19 joint national contracts to buy pharmaceutical products. Some officials believe that the agencies will achieve the bulk of any possible savings simply by sharing pricing data with one another so they can negotiate the lowest prices with pharmaceutical manufacturers and suppliers. Moreover, DoD officials contend that they must maintain their own procurement office to ensure that drug supplies will be available quickly in the event of war.

Other critics, however, might argue that this option would not go far enough. Savings could be even larger if DoD implemented a uniform formulary for all three types of pharmacies that its beneficiaries use: pharmacies at military hospitals and clinics, the mail-order service, and retail pharmacies (where beneficiaries receive partial reimbursement through insurance). DoD officials say that as they have tightened the formularies of drugs available at military facilities, beneficiaries have increasingly turned to retail outlets—which often costs DoD more than if the department had purchased the drugs at federal prices and dispensed them itself. (Consequently, the estimate for this option assumes that DoD's insurance claims for pharmacy services would increase.) If DoD could enforce a single formulary at all pharmacy outlets, it would enjoy more substantial savings.

050-22 Eliminate DoD's Elementary and Secondary Schools

	Savings (Millions of dollars) Budget Authority	Outlays
2001	-10	-9
2002	4	3
2003	20	18
2004	33	31
2005	44	42
2001-2005	90	85
2001-2010	466	456

SPENDING CATEGORY:

Discretionary

The Domestic Dependent Elementary and Secondary Schools (DDESS) system operates schools on several military bases in the United States to educate dependents of military personnel living on those bases. The Department of Defense (DoD) also operates a separate school system for military dependents living overseas.

This option would phase out most of the schools that DDESS runs in favor of increased use of local public schools and would consolidate management of any remaining DDESS schools into the much larger overseas school system. Those changes would save DoD a total of $1.5 billion between 2001 and 2010. Savings for the federal government as a whole would be less—about $400 million through 2010—because the Department of Education would have to spend more on Impact Aid, which it provides to local school districts that enroll dependents of federal employees. (These cost estimates assume that funding for Impact Aid would increase enough that the average amount paid per student living on federal land would remain at its current level.)

Critics would argue that DDESS takes an uneven and largely arbitrary approach to educating the dependents of active-duty service members. The distribution of DDESS schools is mainly a historical accident, dating to the time when segregated public schools in the South did not adequately serve an integrated military. The great majority of military bases in the United States have no DDESS school. And where such schools do exist, they generally enroll only dependents of active-duty members who live on-base; those living off-base, and dependents of civilian employees, are the responsibility of local school districts. In addition, most bases with DDESS facilities offer only elementary and middle schools; high school students living on-base use the public schools. In most of the places where DDESS operates schools, accredited public schools are readily available—with the possible exceptions of Guam, Puerto Rico, and West Point, where DoD would continue to run domestic schools under this option.

Closing DDESS schools need not create major disruptions. The roughly 30,000 students who might be affected already change schools frequently, in large part because they move often as their military parent is reassigned. In many locations, the public school district could continue to use the DDESS facility. (DoD already offers support to some local districts by allowing public schools to operate on-base or providing additional limited funding on a per-student basis.) Finally, to ease the transition, DDESS schools would be phased out at a rate of one per district per year rather than all at once. And the local school districts would receive additional one-time funding and transfer of facilities and equipment to help them absorb their new teaching load.

This option might have several disadvantages, however. First, many parents of DDESS students might be reluctant to see the schools phased out because they believe DoD schools offer higher-quality educations. Second, if local school districts did not maintain the on-base schools, former DDESS students might face longer commutes. Third, some of the savings to the federal government from this option would be offset by increased costs to local school districts. In the past, those districts have effectively been subsidized by not having to pay any of the costs of educating DDESS students while receiving at least some direct and indirect tax revenues from their parents. This option would eliminate that subsidy.

050-23 Consolidate and Encourage Efficiencies in Military Exchange Activities

	Savings (Millions of dollars) Budget Authority	Outlays
2001	62	47
2002	85	76
2003	108	99
2004	111	107
2005	114	112
2001-2005	479	442
2001-2010	1,093	1,048

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATION:

The Costs and Benefits of Retail Activities at Military Bases (Study), October 1997.

The Department of Defense's (DoD's) three military exchange systems—the Army and Air Force Exchange Service, the Navy Exchange Command, and the Marine Corps system—provide a wide array of retail stores and consumer services at military bases. With combined annual sales of approximately $10 billion, operating costs of about $2 billion, and 80,000 employees, the exchanges constitute one of the largest retail businesses in the United States.

The Congress does not directly appropriate funds to the exchanges, but DoD provides them with about $400 million worth of free services each year. Those services include maintaining the exterior of exchange buildings (such as roofs, windows, and heating and cooling systems), transporting goods overseas, and providing utilities at overseas stores. The federal status of DoD exchanges offers other advantages as well: exemption from state and local excise taxes, a monopoly over on-base sales of goods and services, and access to free land and interest-free capital. Those exemptions and other subsidies are worth more than $1 billion a year, the Congressional Budget Office estimates.

Part of that annual subsidy is translated either into lower prices for military personnel and their families or into exchange earnings that support the services' morale, welfare, and recreation (MWR) programs. Another portion is absorbed by inefficiencies. Private retailers in the United States must be efficient to survive in the face of competition. The subsidies that exchanges receive, by contrast, alleviate the pressure of competition and allow the exchanges to operate in ways that private retailers could not afford to. For example, although economies of scale in the private sector often force private retailers to merge, DoD's three exchange systems remain separate—despite numerous studies showing that consolidation would significantly reduce operating costs. Subsidies also distort the incentives that exchange managers face. Because DoD provides free utilities overseas, the Army and Air Force Exchange Service can operate an ice cream production line in Germany without regard to utility costs. And because DoD pays to transport goods overseas, the exchanges can ship beer and carbonated beverages abroad rather than buying them locally.

This option would consolidate the three exchange systems into a single entity and introduce incentives for more efficient operations. Rather than receive DoD support services free of charge, the exchanges would receive a lump-sum appropriation equal to the historical cost of those services and would (like DoD's industrially funded activities) reimburse the providers of those services. Over the long run, consolidating the three exchange systems could save about $65 million a year in overhead costs. Requiring the exchanges to reimburse DoD for support services would save another $40 million a year if it induced the exchanges to reduce the costs of those activities by 10 percent. In all, savings would total $1.1 billion between 2001 and 2010. Initially, the savings might provide additional funding for MWR activities. Over the long run, the increase in exchange earnings would allow DoD to provide its planned level of MWR activities with less support from appropriated funds.

050-24 Increase Competition Between DoD and Private-Sector Housing

	Savings (Millions of dollars) Budget Authority	Outlays
2001	627	32
2002	637	271
2003	648	452
2004	660	540
2005	671	604
2001-2005	3,243	1,899
2001-2010	6,775	5,286

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

050-25

RELATED CBO PUBLICATION:

Military Family Housing in the United States (Study), September 1993.

Most military families receive cash allowances for housing and buy or rent dwellings in the private sector. About one-third, however, live rent-free in on-base housing provided by the Department of Defense (DoD). It costs the federal government about 35 percent more to provide a housing unit than it costs to rent a comparable unit in the private sector. Despite the cost, DoD intends to keep its inventory of housing. The department is experimenting with public/private partnerships that could provide private capital to replace or revitalize on-base housing units, many of which are nearing the end of their service life. But those partnerships are proceeding more slowly than planned, leaving many families in substandard units. Moreover, it is uncertain whether such partnerships will reduce the long-run costs to DoD of providing on-base housing.

This option would reduce the demand for on-base housing by requiring it to compete with private-sector housing. All military families would receive the cash allowance and be free to choose between DoD and private-sector units. DoD—and any companies it takes on as partners—would act like a private landlord, setting rents for on-base units at market-clearing levels (levels at which there would be neither excess vacancies nor waiting lists). On-base housing units would be replaced or revitalized if they met one of two criteria: their value to service members (the market-clearing rent they could command) was sufficient to cover both operating costs and amortized capital costs, or DoD deemed the units indispensable because of their historical nature or importance for military readiness. Those criteria would limit DoD to revitalizing or replacing about 25 percent of its existing housing stock.

The principal advantage of this option would be savings to DoD, which could amount to more than $5 billion in outlays through 2010. The main source of those savings would be lower revitalization and replacement costs as DoD retired aging units rather than investing in ones that could not cover their costs in competition with private-sector housing. Among other advantages, this option would let DoD focus on its warfighting mission rather than on real estate management, eliminate waiting lists for on-base units, and equalize the value of the housing benefits that it provides to families living on- and off-base. Moreover, the housing costs that service members as a whole pay out of pocket would not change: if rents paid to DoD exceeded the housing allowances paid to personnel living in DoD units, the excess would be returned to all service members through an increase in allowance rates.

The main disadvantage of this option is that reducing DoD's role as a provider of housing would limit the benefits associated with the current policy. Advocates argue that housing soldiers and their families on-base promotes esprit de corps, morale, and a sense that the military "takes care of its own." This option would represent a significant break with military tradition. As a result, it could have a negative impact on morale unless it received strong public support from senior military leaders.

On-base units are in high demand among military families primarily because of their low cost to service members. The allowance that families living in DoD housing forfeit equals only about 60 percent of the costs that the federal government incurs in providing a unit. Under this option, families that chose to live on-base would face higher costs than they do today because their rent to DoD would most likely exceed their housing allowance.

050-25 Create Incentives for Military Families to Save Energy

	Savings (Millions of dollars) Budget Authority	Outlays
2001	5	5
2002	26	26
2003	54	54
2004	67	67
2005	68	68
2001-2005	220	220
2001-2010	580	580

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-24 and 050-31

RELATED CBO PUBLICATION:

Military Family Housing in the United States (Study), September 1993.

The Department of Defense (DoD) spent almost $310 million last year on gas, electricity, and water for the approximately 216,000 family housing units that it owns in the United States. DoD's efforts to reduce those costs by promoting resource conservation have met with limited success. One reason is that service members living in DoD-owned housing do not pay for their utilities and may not even know how much gas, electricity, and water they use. Landlords in the private sector have found that utility use typically declines by about 20 percent when tenants are responsible for their own utility bills.

This option would install utility meters in DoD housing units, provide cash utility allowances to the families living there, and then charge for utilities based on actual use. Residents who spent less than their allowance could keep the savings; those who spent more would pay the extra cost out of pocket. The budget for allowances would be set equal to the expected cost of utilities under the new system, or about 80 percent of what DoD now spends. The department would allocate that amount among the different housing units on the basis of their size, energy efficiency, and location. Once the program was established, the allowance budget for each year could be set equal to the previous year's actual utility charges plus an adjustment for inflation. As such, if service members were able to cut their utility usage by more than 20 percent, allowances would fall and the savings from this option would increase. If, however, 20 percent overestimates members' true ability to conserve, allowances would be higher and the savings would be less.

Because families who conserved aggressively would receive more in allowances than they would be charged for utilities, this option would reward people who tried to conserve energy. Families who did not economize would face utility bills in excess of their allowance. However, there is a risk that the allowances for some units might not accurately reflect their characteristics. People living in such a unit might find that the allowance did not cover all of their utility costs even after they had made reasonable conservation efforts.

The principal advantage of this option is that it would reduce DoD's costs by giving military families who live on-base the same incentives for conservation as most homeowners and renters—including military families living off-base. Although DoD would incur the up-front costs of determining allowance amounts, setting up a billing system, and installing meters, this option could provide total savings of about $580 million from 2001 through 2010.

Many DoD housing units already have a connection where a meter could be installed. Nonetheless, a temporary exemption from the metering requirement (and the utility allowances and charges) could be given for some older units if the Secretary of Defense certified that metering them was not feasible.

050-26 Apply Technology to Reduce the Cost of Operating Equipment

	Savings (Millions of dollars) Budget Authority	Outlays
2001	-600	-241
2002	-600	-433
2003	-359	-345
2004	74	-10
2005	600	455
2001-2005	-886	-575
2001-2010	4,625	4,654

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATION:

Paying for Military Readiness and Upkeep: Trends in Operation and Maintenance Spending (Study), September 1997.

In some circumstances, agencies need to spend money to save money. This option would provide an additional $600 million a year to invest in technologies to reduce the operation and maintenance (O&M) costs of weapon systems. The funds would go into "technology insertion accounts" that would be held at the headquarters level of each service and be applied to equipment already used by military units in the field—for example, to support the research, development, procurement, and installation of reliable digital compasses in place of antiquated analog versions, or to replace universal joints on truck axles with constant-velocity joints, which reduce a fleet's tire wear by one-third. Such investments can lessen the need to repair or replace failed components, freeing up maintenance workers and ultimately reducing the costs of operating equipment. Similar opportunities to save on O&M costs without sacrificing performance exist for all of the services' aging weapon systems. Over 10 years, the $6 billion investment in this option could produce $10.6 billion in savings—for net savings of $4.6 billion through 2010.

The services currently spend relatively little on technology insertion. Of the $38 billion spent each year on maintaining weapon systems, only about $600 million is devoted to technology insertion to reduce costs. As an extreme example, the program manager for the M1A1 Abrams tank—the Army's second largest weapon system—received only $1.2 million for research and development (R&D) on ways to reduce the system's $2.9 billion annual operating costs. Studies conducted for the Department of Defense (DoD) by the Logistics Management Institute and others have concluded that funding for technology insertion is inadequate.

The military's current funding for technology insertion programs is limited for three main reasons:

- The services focus their O&M spending on short-term rather than long-term investment. A March 1998 report by the Air Force Materiel Command stated, "The key barrier in today's increasingly tight budgetary environment is finding funding for an activity that will yield net benefits only in the future."

- Technology insertion initiatives typically need small quantities of funds from different appropriations—R&D, procurement, and O&M. But the services are prohibited (partly by Congressional statutes and partly by internal regulations) from using R&D or procurement dollars for components that reduce O&M costs. The dilemma is that officials who want to reduce O&M costs cannot tap into the correct pots of money—R&D or procurement—to do so.

- No incentives exist to encourage technology insertion. Maintenance depots do not have a vested interest in improving the reliability of equipment, because that would reduce their already dwindling workload. Officials who control R&D or procurement funds often focus on the costs not of systems already in the field but of the next emerging weapon system.

This option would promote technology insertion through a combination of new funds and new funding mechanisms. The newly created accounts would be "fenced," or earmarked only for technology insertion, and would contain a blend of R&D, procurement, and O&M funds. Within each service, program managers of weapon systems would compete for access to the funds on the basis of their ability to demonstrate potential gains from technology insertion. Thus, program managers could have the resources to change the O&M costs of their systems. Establishing a separate pool of money for technology insertion would also create incentives within industry to vie for those dollars. If equipment manufacturers, subcontractors, and even depots knew that funding was available for R&D and procurement, they would have an incentive to devise and promote options for reducing O&M costs. Burden-sharing of R&D costs with private industry could increase because more dollars would be available for procuring the new technologies. (Industry officials have stated a willingness to assume the risks associated with research and development, but only if they can be assured of future procurement funding if the R&D is successful.)

The 10-year savings of $4.6 billion estimated for this option assume that each $1 invested in technology insertion yields a return of $3 over five years. The services report a range of returns on such investments, from 3-to-1 to as much as 20-to-1. But the dozens of separate O&M cost-reducing programs now in place suffer from inaccurate accounting of realized savings, so counting on high rates of return might be unrealistic. Many of those programs do not attempt to track the results of technology insertion. To help ensure a high rate of return under this option, project managers would provide account managers with detailed proposals that would include information about the past O&M costs of their systems, estimates of projected savings, and procedures to track and verify those savings.

Although potentially large, the savings under this option are uncertain. And as with any investment, there is a risk that DoD would not receive a good return on the investment. Service leaders claim they cannot absorb many more proposals for R&D or engineering changes without adding personnel to analyze and implement the proposals—thus adding to the cost of technology insertion and reducing the return. In addition, estimated savings might not materialize because reducing the labor force simply because of a labor-saving initiative is often difficult, both politically and practically. Finally, accurate data on costs and savings are not readily available, further clouding claims of gains made.

Each of the services is currently reforming its programs to account for the life-cycle costs of weapon systems, which could help better identify savings, but those efforts are not closely tied to technology insertion programs. Therefore, some observers argue that DoD should wait until the services can track costs better before offering additional funds to reduce costs.

050-27 Close and Realign Additional Military Bases

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	0	0
2003	0	0
2004	-558	-173
2005	-1,189	-570
2001-2005	-1,747	-743
2001-2010	4,666	1,099

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

050-28 and 050-29

RELATED CBO PUBLICATIONS:

Review of *The Report of the Department of Defense on Base Realignment and Closure* (Letter), July 1998.

Closing Military Bases: An Interim Assessment (Paper), December 1996.

Beginning in the late 1980s, the Department of Defense (DoD) sought to reduce its operating costs by closing unneeded military bases. Significant reductions in force structure at the end of the Cold War made many bases unnecessary. Because political and procedural difficulties had long made closing bases nearly impossible, the Congress set up four successive independent commissions on base realignment and closure (or BRAC). Those commissions recommended shutting or realigning (moving departments and facilities at) hundreds of military installations in the United States, Puerto Rico, and Guam. When all of the actions from the four BRAC rounds are completed, DoD will save about $5.6 billion a year in operating costs, it estimates.

This option would authorize two additional rounds of base closures and realignments in 2003 and 2005. In the long run, such actions can produce substantial savings. However, they require some up-front investment, so costs would increase in the short run. Between 2001 and 2010, this option would reduce DoD's costs by a net total of $4.7 billion. Beginning in 2012, the department could realize recurring savings of around $4 billion per year. Those estimates are based on DoD's experience and current projections for the four earlier rounds of base closings. (The estimates do not include the costs of environmental cleanup, since DoD is obligated to incur such costs regardless of whether it operates or closes bases.)

Closing and realigning additional military bases is consistent with DoD's overall drawdown of forces. By several measures, planned force reductions significantly exceed the projected decrease in base capacity. For example, the department intends to cut the number of military and civilian personnel by 34 percent from the 1990 level. But according to DoD, only 21 percent of the base infrastructure in the United States has been eliminated.

The Secretary of Defense asked the Congress in early 1998 and again in early 2000 to authorize two more rounds of base closures. In *The Report of the Department of Defense on Base Realignment and Closure* of April 1998, DoD stated that opportunities exist for further cutbacks and consolidations at several types of bases—such as defense laboratories, test and evaluation installations, training facilities, naval bases, aircraft installations, and supply facilities.

Some analysts, however, argue that the BRAC cuts have gone far enough in matching the planned reductions in forces. The base structure, they say, should retain enough excess capacity to accommodate new risks to national security that could require a surge in the number of military forces. Opponents of more closures also cite the possible adverse economic effects on local communities. Some opponents suggest that savings could be made by demolishing certain buildings or by achieving other operating efficiencies short of closing bases.

050-28 Demolish Excess and Obsolete Structures

	Savings (Millions of dollars) Budget Authority	Outlays
2001	-30	-21
2002	-23	-23
2003	-15	-17
2004	22	11
2005	23	21
2001-2005	-23	-28
2001-2010	98	93

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

050-27

The defense drawdown has left many military bases with structures that the services no longer need and that have no remaining asset value. Those structures include buildings, such as schools and family housing units, as well as other facilities, such as piers and runways. In some cases, the structures are dangerous eyesores. In other cases, their availability attracts marginal users who benefit from occupying them because the users are not required to pay the full costs of the utilities and other support that the bases provide. Although demolishing those structures would entail up-front spending, it would allow the Department of Defense (DoD) to avoid future maintenance costs. Estimates by DoD suggest that demolition projects may pay for themselves in as little as five years.

This option would increase funding to tear down excess, obsolete structures by $35 million a year over the 2001-2003 period. A majority of those annual funds, $30 million, would be allocated to the services' operation and maintenance (O&M) accounts to fund the demolition of excess facilities that are maintained with O&M dollars. The remaining $5 million would be allocated to the family housing accounts to pay for demolishing obsolete family housing units that are too costly to repair. Those funds would allow DoD to increase demolitions by 6 percent from planned levels and would generate $22 million in annual savings after 2003.

The services expect to tear down 80 million square feet of buildings by 2003 in accordance with a management reform that the Office of the Secretary of Defense (OSD) began in 1997. Recent defense plans have extended the Air Force's and Navy's demolition programs to 2005 to accommodate their large inventories of structures other than buildings. DoD plans to spend a total of $773 million on demolition programs during the 2000-2003 period, with an estimated savings in O&M costs of $160 million a year after that.

However, DoD officials maintain that the department's inventory of real property will still contain excess structures, such as buildings and other facilities that are maintained with O&M dollars, after the current demolition programs are completed in 2005. Funding above planned levels would be necessary to demolish the rest of those excess structures and generate additional O&M savings. In addition, current OSD plans do not fund the destruction of excess, obsolete family housing units. Although the services' family housing commands have adopted demolition as a key tool in their strategies for real property management, critics argue that the resources devoted to those activities are inadequate.

The primary disadvantage of this option is that the quantity of structures that are both excess and obsolete is unclear. If DoD has underestimated its requirements for facilities, demolition programs may destroy a structure that has a potential use in the future. One alternative to demolition is to board up a facility and cease maintaining it. Nonetheless, as long as structures remain in DoD's inventory, the department is likely to feel pressure to maintain them and make them available to potential users.

050-29 Consolidate Depot Functions and Close Some Facilities

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	-386	-120
2003	-243	-111
2004	-94	-32
2005	311	54
2001-2005	-411	-208
2001-2010	1,232	1,234

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-27 and 050-30

RELATED CBO PUBLICATION:

Public and Private Roles in Maintaining Military Equipment at the Depot Level (Study), July 1995.

Despite four rounds of base realignment and closure (BRAC), the services still have a large number of underutilized buildings and equipment within their network of maintenance depots (government-owned and -operated industrial facilities that repair military equipment). The individual services, the Office of the Secretary of Defense, and the General Accounting Office (GAO) have all recommended closing additional depot facilities to reduce that excess capacity, which GAO has estimated at about 50 percent and rising.

This option would authorize a BRAC commission that would focus exclusively on maintenance depots. Assuming the commission identified up to five facilities for closure, this option could save a total of $1.2 billion between 2001 and 2010. Closing additional depots would require some up-front investment, but the Department of Defense (DoD) would probably break even within five to six years.

When the actions recommended by the four previous BRAC rounds are completed next year, 19 of the 38 major government-owned and -operated depots that existed in 1988 will no longer be functioning as government entities. Nevertheless, the depot network will still have excess capacity because its workload is declining for four reasons: the overall military force structure and stocks of weapons and equipment continue to be reduced, most new or modified weapon systems are more reliable than previous systems, manufacturers of weapon systems are seeking greater control over maintenance support for their systems, and some unit commanders are conducting more repairs in their own local maintenance facilities (see option 050-30).

Proponents of a BRAC commission specifically for maintenance depots would argue that the unique characteristics of depots—including nondeployable personnel, huge fixed capital assets, and a mostly civilian workforce—set them apart from conventional military bases. In that view, the special expertise required to understand depot-industry issues—to determine to what extent repairs could be made more efficiently in the private sector and to define and identify excess capacity from an overall DoD perspective—underscores the need for a specialized BRAC panel whose members have knowledge of the unique attributes of the depot system. (That argument could also apply to the defense laboratories, research facilities, and test and evaluation facilities.)

Opponents of this option, by contrast, might argue that depot realignments and closures have gone far enough. Many critics feel that DoD should retain enough capacity within its depot system to accommodate new risks to national security that could require a surge in depot-level maintenance. In addition, depot closures could have adverse economic effects on local communities—at least in the short run.

Instead of closing more depots, opponents would argue, DoD could reduce excess capacity by entering into public/private partnerships that utilized that capacity during peacetime and thus made depots more cost-effective. For example, the commercial aviation industry reportedly faces a shortfall in its depot capacity and could potentially become a partner in sharing the costs of maintaining military depots.

050-30 Change the Management and Pricing of Repairs

	Savings (Millions of dollars) Budget Authority	Outlays
2001	46	35
2002	154	125
2003	735	586
2004	403	447
2005	352	370
2001-2005	1,691	1,563
2001-2010	3,434	3,321

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-29

When subcomponents of weapon systems (such as transmissions and radars) break down, unit commanders often have them repaired in the unit's own maintenance and repair shops—called intermediate maintenance facilities, or general support facilities in the Army. That is the case even if it would be less costly for the Department of Defense (DoD) as a whole if the subcomponents were sent to large, centralized maintenance facilities—called depots—for repair.

This option would reduce costs by changing the way in which DoD manages and charges for repair of those subcomponents—known as depot-level repairables (DLRs). Under this option, repair work for DLRs would be allocated to either depots or intermediate facilities by managers who were aware of the full costs of both sources of repair and had an incentive to minimize DoD's total repair bill. Such a system could save the department $3.4 billion over 10 years through improving inventory efficiency alone.

In the early 1990s, DoD tried to reduce the demand for repairs and make unit commanders more careful in their use of DLRs by shifting repair funds out of central accounts and into the budgets of individual units. To a large degree, the plan succeeded: demand for repair and replacements of DLRs declined. But because of problems in the price structure for repairs, shifting financial responsibility to unit commanders had unintended consequences. The prices that depots charge for DLRs overstate the actual cost of doing repairs because depots must cover their overhead and management costs. By contrast, some of the costs that intermediate facilities face (including the costs of capital and military labor) are not included in the prices that units pay. Thus, commanders have a financial incentive to repair DLRs in their own facilities regardless of the actual cost, and repair jobs that before would have gone to a depot are being handled by intermediate facilities. According to one joint Navy/Office of the Secretary of Defense study, intermediate maintenance is up to twice as expensive as depot repairs. Because intermediate facilities are not as well equipped for some tasks as depots, repairs could take longer or have higher failure rates. Besides raising costs, the shift in workload has increased excess capacity in the depots and may have decreased the quality of repairs overall.

This option would try to improve the distribution of the DLR workload between depots and intermediate maintenance facilities by centralizing management of DLRs. More important, it would provide a pricing system that more accurately reflects the actual cost of repairs. Within each service, equipment (or item) managers would assume control of all DLR inventories and allocate repairs between depots and intermediate facilities. They, not unit commanders, would decide which source of repair was less costly. Commanders would have a single point of contact—the item manager—for each type of DLR, regardless of whether the work had been allocated to an intermediate facility or a depot.

Under this option, both depots and intermediate facilities would charge item managers for repairs. Each repair facility would set its prices to cover only those costs that varied with the DLR workload, taking into account the time to complete the work, quality, and return of broken DLRs. In other words, it would cover the additional costs that would be incurred for each specific repair, such as materials, labor, and transportation. That pricing structure has been proposed by economists at RAND, the Center for Naval Analyses, and elsewhere. By encouraging item managers to send DLRs to the facility that could do the work at the lowest cost, it would let DoD minimize its total repair bill.

Intermediate facilities would continue to rely on direct appropriations to cover their fixed capital and overhead costs. In addition, military personnel who would deploy as part of maintenance units in wartime could continue to be assigned to intermediate facilities in peacetime and be paid from their service's central military personnel account. However, costs that varied with the amount of repair work at the intermediate facility would be covered not through direct appropriations but through the prices charged for DLR repairs. Those costs would include the salaries of civilian workers and military personnel whose positions were required not because of wartime deployments but because of the DLR repair workload in peacetime. In turn, the intermediate maintenance facilities would be required to reimburse the services' military personnel accounts for those salaries.

In the case of depots, repair costs that did not vary with workload would be paid by customers through a flat charge that did not depend on how much work they sent to the depot that year. Such a two-part pricing system—a flat charge plus a variable fee based on workload—is similar to the system that some telephone companies use. Costs that were not related to ongoing repair tasks but were previously included in DLR prices would be covered by direct appropriations. For example, the costs of maintaining excess facilities for wartime, such as the Army's Watervliet facility (a unique plant that manufactures large gun barrels), would not be charged to depot customers. That approach to pricing would allow the depot to cover its total costs but not charge more for an additional task than the task would cost to perform. A study by RAND concluded that such an approach would reduce the prices that depots charge for repairs. A price reduction could shift a significant amount of the DLR workload back to depots.

One disadvantage of this option is that commanders would have less control over their intermediate maintenance facilities. Thus, it would be harder for them to ensure that those facilities provided an adequate minimum number of personnel to cover wartime tasks or to support deployments and contingency operations. In addition, centralization and worldwide management of the DLR inventory would require new software and computer systems.

Another disadvantage is that developing appropriate prices for the depots and intermediate facilities could prove difficult. Depot managers, anxious to attract work by keeping their prices as low as possible, might try to move costs into the flat charge or direct appropriations that were in fact part of the costs of repair that varied with workload. Alternatively, depot managers might be reluctant to separate repair costs that varied with workload from those that were fixed because doing so would highlight their degree of excess capacity. In addition, an accurate historical database of repair costs at intermediate facilities does not exist, which makes pricing DLR repairs there difficult.

A more fundamental concern is that it might be difficult to predict exactly how managers would respond to the new prices. (DoD, for example, failed to predict how managers would respond to the current DLR pricing scheme.) The unintended consequences of changing prices could outweigh the benefits if this option was not implemented carefully and systematically. Opponents of this option might argue that it would be simpler for DoD to just order work to go to the facility that could perform it at the least cost. Supporters might counter that DoD already has rules about where DLRs are to be repaired but that current DLR prices are driving units to ignore those rules.

050-31 Allow Federal Agencies to Bargain for Electricity

	Savings (Millions of dollars) Budget Authority	Outlays
2001	36	36
2002	128	128
2003	90	90
2004	28	28
2005	23	23
2001-2005	307	307
2001-2010	422	422

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

050-25 and 270-07

RELATED CBO PUBLICATIONS:

Electric Utilities: Deregulation and Stranded Costs (Paper), October 1998.

Should the Federal Government Sell Electricity? (Study), November 1997.

The federal government spends more than $2 billion per year in the United States on electricity, of which about 50 percent is purchased through the Department of Defense. Although the government is a large consumer of electricity, it pays full retail prices. A provision in a continuing appropriation act for fiscal year 1988 (Public Law 100-202, section 8093) requires federal agencies to conform to state laws regarding electricity purchases. Some states have already allowed retail customers to choose their electricity supplier and negotiate lower prices.

This option would let the federal government realize such savings in all states, regardless of state regulations on retail customers. The resulting savings could total around $422 million over 10 years if agencies' appropriations were reduced by the expected decrease in electricity bills. (The lower savings in 2001 reflect phase-in and transition costs.)

The federal government would face lower electricity prices if it purchased power on a competitive basis. In that situation, suppliers would have an incentive to provide electricity at the lowest possible cost and offer new services. Under traditional regulation, utilities generally gave customers the same product: reliable electricity at a fairly high, but uniform, price. If the federal government was allowed to negotiate for electricity, suppliers would be encouraged to furnish a greater variety of electricity services—with different prices and different degrees of reliability, depending on what the federal government wanted or needed. Some states, such as California, Massachusetts, Pennsylvania, and Rhode Island, have already introduced retail competition, allowing all retail customers—including federal agencies—to choose their electricity provider. Any reduction in federal spending because of Congressional action would have to take into account that those states already allow price competition and others will allow it before 2010.

Several bills to restructure the electricity industry were introduced in the 105th Congress. They would have allowed all customers, not just the federal government, to buy electricity in a competitive market. A comprehensive electricity-restructuring bill like one of those may be needed for the federal government to realize all of the savings from negotiating lower prices for electricity. Otherwise, an electricity provider that once served the federal government might be reluctant to lose so large a customer and could try to impede the government's choice of suppliers. (In some parts of the country, no alternative suppliers may be available.) Also, the federal government could be subject to surcharges if it broke a contract with its old supplier. Such surcharges would diminish the savings from this option. The federal government might also be perceived as unfair if it was allowed to choose suppliers but no other retail customer was. Prices to other consumers could rise if the federal government chose a new supplier and the utility that once served it could not search for alternative buyers for the electricity.

050-32 Sell Surplus Real Property of the Department of Energy

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	3	3
2003	3	3
2004	3	3
2005	3	3
2001-2005	12	12
2001-2010	17	17

SPENDING CATEGORY:

Mandatory

The Department of Energy (DOE) controls about 2.4 million acres of land, much of it surrounding sites in the West and Southeast that have contributed to the nation's efforts to develop nuclear weapons. DOE's Office of Inspector General (IG) recently identified 309,000 acres that it considers no longer essential to carrying out the department's core missions of weapons dismantling, environmental cleanup, technology development, and scientific research. That acreage is part of the Oak Ridge Reservation in Tennessee, the Hanford Site in Washington, and the Idaho National Engineering Laboratory. Additional real property that may be excess but was not evaluated in the IG report exists at such DOE facilities as the Nevada Test Site, the Los Alamos National Laboratory in New Mexico, the Fermi National Accelerator Laboratory in Illinois, and the Savannah River Site in South Carolina.

To demonstrate the potential savings from disposing of those properties, this option would require DOE to sell at market value 16,000 acres at the Oak Ridge Reservation that the IG has identified as excess. (The IG proposed transferring other excess property to the Department of the Interior for management as a natural resource.) That sale—conducted over four years to minimize the effect on local land values—could yield savings of $17 million during the 2001-2010 period, including reduced outlays for property management. That sum excludes any savings associated with reducing DOE's liabilities for payments to local governments in lieu of taxes or the costs of cleaning up future accidents. The estimate also assumes that the sale would be exempted from requirements of the Federal Property Administrative Services Act to first offer surplus property to state and local governments.

Opponents of selling excess land argue that DOE's mission is changing to include the stewardship of land as a valuable national resource. Most of the acreage in question was used as buffer lands and has been little touched in the past 50 years. In line with the land's unique qualities, DOE has established environmental research parks at seven of its properties to protect species and cultural sites and to provide a natural laboratory for research and environmental monitoring. It has also made agreements with the Fish and Wildlife Service and the Bureau of Reclamation to manage certain areas. Moreover, some of the land (excluding the acres at Oak Ridge to be sold in this option) may be contaminated by hazardous materials or unexploded ordnance, which would have to be disposed of before transfer could occur. (Such disposal would diminish the savings from this option.) In addition, DOE still needs buffer lands to control the future spread of contaminants from its nuclear sites.

Proponents argue that selling unneeded DOE property would not only save money but also make the land available for more uses, including agriculture, recreation, and residential or commercial development. They note that according to the IG, cleanup will be necessary at only a small part of the excess acreage. Moreover, the government would still have to pay cleanup costs if it kept or transferred the property rather than selling it.

050-33 Eliminate Cargo Preference

	Savings (Millions of dollars) Budget Authority	Outlays
2001	177	148
2002	272	252
2003	371	351
2004	380	374
2005	389	387
2001-2005	1,589	1,511
2001-2010	3,679	3,589

SPENDING CATEGORY:

Discretionary

The Cargo Preference Act of 1904 and other laws require that U.S.-flag vessels be used to carry certain government-owned or government-financed cargo that is shipped internationally. Eliminating cargo preference would lower federal transportation costs by allowing the government to ship its cargo at the lowest available rates. That would reduce the government's costs by $177 million in 2001 and a total of almost $3.7 billion over the next decade.

Two federal agencies—the Department of Defense (DoD) and the Department of Agriculture (USDA)—account for about 90 percent (by weight) of the government shipments subject to cargo preference laws. The preference applies to nearly all DoD freight and three-quarters of the USDA's shipments of food aid, as well as shipments associated with programs of the Agency for International Development and the Export-Import Bank. Roughly 70 percent of the savings from eliminating cargo preference would come from defense discretionary spending, with the other 30 percent from nondefense discretionary spending.

Supporters of cargo preference argue that it promotes the economic viability of the nation's maritime industry. That industry has suffered at the hands of foreign competition in recent decades. Under federal law, U.S. mariners must crew U.S. vessels, and in general, U.S. shipyards must build them. Because U.S.-flag ships face higher labor costs and greater regulatory responsibilities than foreign-flag ships, they generally charge higher rates. Without guaranteed business from cargo preference, many U.S.-flag vessels still engaged in international trade would leave the fleet. They would do so either by reflagging in a foreign country to save money or by decommissioning if they could not operate competitively. Supporters also argue that cargo preference helps bolster national security by ensuring that U.S.-flag vessels and U.S. crews are available during wartime. Finally, eliminating cargo preference could cause U.S. ship operators and shipbuilders to default on loans guaranteed by the government. (The possibility of such defaults is not reflected in the estimated savings for this option.)

Critics of cargo preference say it represents a subsidy of private industry by taxpayers, which simply helps a handful of carriers preserve their market share and market power. In 1999, the program cost was nearly $1 million per vessel for the 475 ships, barges, and tugboats benefiting from the program. Opponents also point out that even DoD officials question the national security importance of the Merchant Marine fleet. DoD has invested in a fleet of its own specifically for transporting military equipment. It also contracts with foreign-flag ships when needed. In addition, critics of cargo preference argue that the U.S. government is at a competitive disadvantage in selling surplus agricultural commodities abroad because it must pay higher costs to transport them.

150

International Affairs

Budget function 150 covers all spending on international programs by various departments and agencies whose missions concern international affairs. The category includes spending by the Department of State to conduct foreign policy and exchange programs, funds controlled directly by the President to give other nations economic and military aid, and U.S. contributions to international organizations such as the United Nations, multilateral development banks, and the International Monetary Fund. Function 150 also includes financing for exports through the Export-Import Bank. CBO estimates that discretionary outlays for the function will total $20.1 billion in 2000. Repayments of loans and interest income in the Exchange Stabilization Fund account for the negative balances in mandatory spending for this function. Discretionary appropriations for international affairs hovered around the $20 billion level throughout the 1990s.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	20.0	21.3	20.9	33.3	20.9	20.2	18.1	18.2	19.0	41.5	22.1
Outlays											
Discretionary	19.1	19.7	19.2	21.6	20.8	20.1	18.3	19.0	18.1	19.5	20.1
Mandatory	-5.2	-3.8	-3.1	-4.3	-3.7	-3.7	-4.8	-3.8	-5.0	-4.3	-3.9
Total	13.9	15.9	16.1	17.2	17.1	16.4	13.5	15.2	13.1	15.2	16.2
Memorandum:											
Annual Percentage Change in Discretionary Outlays		3.4	-2.7	12.6	-3.5	-3.3	-8.8	3.5	-4.6	7.8	3.2

150-01 Eliminate Overseas Broadcasting by the U.S. Government

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	247	321
2002	263	297
2003	323	313
2004	395	338
2005	410	372
2001-2005	1,638	1,641
2001-2010	3,688	3,673
Relative to WIDI		
2001	261	332
2002	288	319
2003	360	347
2004	444	385
2005	472	432
2001-2005	1,825	1,815
2001-2010	4,382	4,338

SPENDING CATEGORY:

Discretionary

Several entities provide U.S. overseas broadcasting. Radio Free Europe (RFE) and Radio Liberty (RL) broadcast country-specific news to Eastern Europe and the former Soviet Union, respectively. The Voice of America (VOA) oversees radio broadcasts that provide news and U.S.-related information to audiences worldwide. The State Department oversees television broadcasting services similar to VOA's radio broadcasts and also manages a broadcasting service to Cuba. In 1996, the Congress consolidated the appropriations for VOA, RFE/RL, and television and film service into the international broadcasting operations account. Funding for radio and television broadcasting to Cuba and for construction of broadcast facilities was provided in separate appropriations.

This option would eliminate VOA and RFE/RL and end broadcasting services to Cuba, all overseas construction of broadcast facilities, and U.S. overseas television broadcasting. Compared with the funding level in 2000, those cuts would save almost $3.7 billion over 10 years. (The savings are net of the near-term costs of termination, such as severance pay for employees.)

Proponents of ending overseas broadcasting by the U.S. government say that RFE/RL and VOA are Cold War relics that are no longer necessary. RFE and RL continue to broadcast to former Communist countries in Europe even though those countries now have ready access to world news. With the advent of satellite television broadcasting, most nations can receive news about the United States and the world from private broadcasters, such as the Cable News Network (CNN). Some proponents of termination also argue that the primary technology used by VOA and RFE/RL—shortwave radio—limits the audiences and thus the effectiveness of U.S. overseas broadcasting. In addition, proponents maintain that foreigners may distrust the accuracy of broadcasts sponsored by the U.S. government.

Critics of this option would argue that the current level of broadcasting should continue or even increase. The process of change in Eastern Europe and the former Soviet Union needs nurturing, they say, and U.S. broadcasting can help in that process. In addition, many countries in other parts of the world remain closed to outside information. Supporters of VOA and RFE/RL argue that shortwave radio is the best way to reach audiences in closed countries because very few people there own satellite dishes, which are needed to receive television broadcasts such as those of CNN. Moreover, they note, VOA and RFE/RL are broadcasting more programs over AM and FM frequencies. Supporters of U.S. government broadcasting also argue that it should be sharply increased to some countries, such as China and North Korea. Further, they maintain that television is a powerful communications tool, and private television networks cannot adequately communicate U.S. policy and viewpoints.

150-02 Reduce Assistance to Israel and Egypt

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	1,505	483
2002	1,665	1,070
2003	1,825	1,536
2004	1,985	1,899
2005	2,145	2,054
2001-2005	9,125	7,043
2001-2010	21,770	19,295
Relative to WIDI		
2001	1,586	528
2002	1,825	1,178
2003	2,071	1,719
2004	2,319	2,165
2005	2,566	2,405
2001-2005	10,367	7,995
2001-2010	26,484	23,339

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATIONS:

The Role of Foreign Aid in Development (Study), May 1997.

Enhancing U.S. Security Through Foreign Aid (Study), April 1994.

Limiting Conventional Arms Exports to the Middle East (Study), September 1992.

As part of the 1979 Camp David peace accords, the United States agreed to provide substantial amounts of aid to Israel and Egypt to promote economic, political, and military security. That aid, which for years totaled $5.1 billion for the two countries, is paid through the Economic Support Fund (ESF) and the Foreign Military Financing (FMF) program. Of that total, Israel received $3 billion ($1.2 billion in ESF payments and $1.8 billion from the FMF program), and Egypt received $2.1 billion ($815 million from the ESF and $1.3 billion from the FMF program).

In January 1998, Israel proposed phasing out its $1.2 billion a year in ESF payments while increasing its FMF assistance by $600 million a year. The conference report for the 1999 Foreign Operations Appropriations Act endorsed that proposal with a 10-year phase-in. As a result, it cut ESF aid to Israel by $120 million and increased FMF aid by $60 million. The conference report also reduced economic assistance to Egypt from $815 million in 1998 to $775 million in 1999—and proposed cutting it to $415 million by 2008—while keeping military aid constant.

This year, U.S. aid to the two nations will total $6.1 billion (including $1.2 billion in FMF aid to Israel promised for implementing the Wye peace accords). That amount represents more than three-fourths of discretionary spending for U.S. security assistance and more than 40 percent of the foreign operations budget for 2000.

This option would drop the one-time funding for implementing the Wye peace accords and forgo the proposed increase in military funding for Israel (maintaining that aid at its 1998 level). The option would also continue to cut economic assistance to both Israel and Egypt each year through 2008. The reductions in Israeli aid would save $481 million in 2001, compared with this year's funding level, and a total of $6.7 billion over five years and almost $17.8 billion over 10 years. Adding in the cuts to Egyptian aid would bring total savings in outlays to $483 million in 2001, $7.0 billion over five years, and $19.3 billion over 10 years.

The conference report asserted that increased military assistance to Israel was necessary because "the [country's] security situation, particularly with respect to weapons of mass destruction, has worsened." But despite reports of weapons technology being transferred to Iran, critics could argue that Israel's security situation has improved. Iraq's arsenal of weapons of mass destruction has been reduced, though not eliminated, by U.N. inspections; Israel has concluded a peace treaty with Jordan; and peace talks with the Palestinians and Syrians are continuing. In addition to those developments, Israel's per capita income (in excess of $18,000) approaches that of the United States' European allies, who have long been prodded by the Congress to assume greater responsibility for their own defense.

As for Egypt, some analysts say U.S. assistance to that country is not being spent wisely or efficiently. Critics note that high levels of appropriations have exceeded Egypt's ability to spend the funds, leading to the accumulation of large undisbursed balances, inefficient use of assistance, and delays in making the reforms needed to foster self-sustaining growth. Furthermore, many other countries and organizations contribute substantial amounts of money to Egypt, which could make reducing U.S. assistance more feasible.

150-03 Eliminate the Export-Import Bank, Overseas Private Investment Corporation, and Trade and Development Agency

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	814	155
2002	817	457
2003	809	577
2004	808	659
2005	808	696
2001-2005	4,056	2,544
2001-2010	8,096	6,158
Relative to WIDI		
2001	829	158
2002	847	470
2003	855	601
2004	872	698
2005	888	749
2001-2005	4,290	2,676
2001-2010	8,995	6,788

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

350-02, 350-08, and 350-09

RELATED CBO PUBLICATIONS:

The Domestic Costs of Sanctions on Foreign Commerce (Study), March 1999.

The Role of Foreign Aid in Development (Study), May 1997.

The Export-Import Bank (Eximbank), the Overseas Private Investment Corporation (OPIC), and the Trade and Development Agency (TDA) promote U.S. exports and overseas investment by providing a range of services to U.S. companies wishing to do business abroad. Eximbank offers subsidized direct loans, guarantees of private lending, and export credit insurance; OPIC provides investment financing and insurance against political risks; and TDA funds feasibility studies, orientation visits, training grants, and other forms of technical assistance. Appropriations in 2000 for Eximbank, OPIC, and TDA are $814 million, $59 million, and $44 million, respectively.

Those organizations are only three of the various U.S. government agencies (some of which are part of the Department of Agriculture) that promote trade and exports. Moreover, their impact on exports may be limited. According to the annual reports of OPIC, Eximbank, and TDA, those three agencies supported about 2 percent of total U.S. exports in 1995.

This option would eliminate TDA and the subsidy appropriations for Eximbank and OPIC. The latter two agencies could not make any new finance or insurance commitments but would continue to service their existing portfolios. Those changes would save $155 million in outlays in 2001, $2.5 billion through 2005, and almost $6.2 billion over 10 years compared with the funding level for 2000.

Supporters of promoting exports argue that those agencies play an important role in helping U.S. businesses, especially small businesses, understand and penetrate overseas markets. They level the playing field for U.S. exporters by offsetting the subsidies that foreign governments provide to their exporters, thereby creating jobs and promoting sales of U.S. goods. By encouraging U.S. investment in areas such as Russia and the states of the former Soviet Union, those agencies may also serve a foreign policy objective.

Critics dispute the claim that promoting exports creates U.S. jobs. They assert that by subsidizing exports, the government distorts business decisions that are best left to free markets. OPIC and Eximbank finance programs that have trouble raising funds on their own merit. Similarly, those agencies' insurance programs may encourage moral hazard—the practice of companies investing in riskier projects than they would if more of their own funds were at stake. Finally, critics argue, those agencies encourage highly risky projects in vulnerable areas. Although emerging economies like Russia and Indonesia may be important markets for U.S. exports, they can also be dangerous: firms operating there may face considerable political, currency, and business risks.

250

General Science, Space, and Technology

Budget function 250 includes funding for the National Science Foundation, more than 90 percent of the spending of the National Aeronautics and Space Administration, and funding for general science research by the Department of Energy. In 2000, CBO estimates, outlays for function 250 will total about $18.5 billion. For the past 10 years, the trend in spending for the function has generally been upward.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	14.5	16.5	17.3	17.2	17.6	16.7	16.7	16.6	18.0	18.8	19.1
Outlays											
Discretionary	14.4	16.1	16.4	17.0	16.2	16.7	16.7	17.1	18.2	18.1	18.4
Mandatory	0	0	0	0	0	0	0	0	0	0	0.1
Total	14.4	16.1	16.4	17.0	16.2	16.7	16.7	17.2	18.2	18.1	18.5
Memorandum:											
Annual Percentage Change in Discretionary Outlays		11.6	1.8	3.9	-4.9	3.2	-0.1	2.8	6.0	-0.5	1.8

250-01 Cancel the International Space Station Program

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	1,323	913
2002	2,323	1,987
2003	2,323	2,303
2004	2,323	2,323
2005	2,323	2,323
2001-2005	10,615	9,849
2001-2010	22,230	21,464
Relative to WIDI		
2001	1,345	928
2002	2,400	2,046
2003	2,441	2,407
2004	2,483	2,469
2005	2,525	2,511
2001-2005	11,194	10,361
2001-2010	24,475	23,569

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATION:

Reinventing NASA (Study), March 1994.

The first two elements of the international space station were launched and joined in late 1998. The launch of a third element using a Russian Proton rocket has been delayed pending the investigation of an October 1999 failure of that launcher. The space shuttle has also encountered delays recently, suggesting that the completion date currently planned for the facility—2005— could be at risk. By that time, an estimated $25 billion will have been spent to develop, build, and assemble the space station. The General Accounting Office (GAO) estimates that the life-cycle cost of the entire project, including operation, maintenance, and transportation to and from orbit, will be over $95 billion. The Congress's yearly decision about whether to continue funding for the program hinges not on the money already spent but on whether the program's benefits are sufficient to justify spending an additional $70 billion through 2013.

People who would cancel the international space station program assert that its benefits are unlikely to justify additional spending and that costs are likely to increase above those estimated by GAO. To support their position, critics cite the general lack of enthusiasm for the space station among individual scientists and scientific societies. The program's opponents also note that the costs of the program have continually increased, although its capabilities and scope have decreased. Critics point as well to the uncertainty surrounding the costs of operating and supporting the facility once it has been developed and launched. Regarding that issue, opponents are skeptical of the National Aeronautics and Space Administration's assurance that the station's operating costs will be low, noting that the agency made similar claims about the space shuttle that proved overly optimistic.

Advocates of continued spending for the space station reject critics' claim that the program's benefits do not sufficiently justify its costs. Supporters place a high value on the role of the station as a stepping-stone to future human exploration of the solar system. They also contend that the program will deliver both scientific advances and perhaps even commercial benefits. Supporters further argue that Russia's participation has strengthened the foreign policy reason for continuing the program. They assert that drawing Russia, and particularly its aerospace industry, into a cooperative venture will help to stabilize the Russian economy and provide incentives for Russia to adhere to international agreements on the spread of missile technology. Advocates also point out that the project's cancellation would force the United States to renege on agreements signed with European nations, Japan, and Canada. That could hurt the prospects for future international cooperative agreements on space, science, and other areas of mutual interest.

250-02 Eliminate the Experimental Program to Stimulate Competitive Research

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	122	37
2002	152	101
2003	152	133
2004	152	143
2005	152	148
2001-2005	730	562
2001-2010	1,490	1,322
Relative to WIDI		
2001	124	37
2002	157	103
2003	160	137
2004	163	151
2005	166	159
2001-2005	770	587
2001-2010	1,640	1,442

SPENDING CATEGORY:

Discretionary

The Experimental Program to Stimulate Competitive Research (EPSCoR), a partnership between states and several research-oriented federal agencies, was designed to encourage more investment by states in science and technology. EPSCoR was created in response to a concentrated distribution among the states of federal research and development (R&D) funding: a large number of states receive little funding. Currently, federal agencies spend about $113 million on EPSCoR.

Eighteen states and the Commonwealth of Puerto Rico currently take part in EPSCoR. Between 1980 and 1998, the National Science Foundation provided roughly $270 million to more than 60 colleges, universities, and laboratories that had not received significant federal R&D funding in the past. State governments, local industry, and other nonfederal sources provided an additional $300 million to those institutions. The entire effort has supported 2,000 scientists and engineers.

Opponents of EPSCoR contend that the nation must make optimal use of its limited research dollars. That principle would argue for supporting researchers whose proposals are judged superior through a process of peer review, without regard to geographical distribution. Furthermore, critics doubt whether newcomers to the research enterprise can sustain a top-level effort, which requires substantial ongoing investments by the states and regional institutions. Even with matching funds from the states and other nonfederal organizations, novice research institutions might find it difficult to succeed.

Critics also argue that EPSCoR was supposed to be an experimental program, not a permanent source of R&D support for selected states. They note that after nearly 15 years of EPSCoR support, the program's recipients continue to attract only about 8 percent of the federal funding for academic R&D. Opponents point to the corresponding lack of improvement in state shares of such funding: participating states that began the 1980s in the bottom half of the national rankings were still in the bottom half in 1998.

Advocates maintain that EPSCoR promotes a more equitable geographic distribution of the nation's science and technology base. They assert that state policymakers invest more in R&D than they would without EPSCoR's incentives and those investments promote equity in higher education by giving students in those states the research experience and training necessary for careers in scientific fields. Proponents also contend that the program fosters technology-related industries in the states by involving local firms in selecting research topics. Supporters note that 15 of the EPSCoR states experienced above-average growth in federal funding for academic R&D over the 1990-1998 period. They claim that the EPSCoR states have improved their rankings in their chosen "niche" fields, even if such changes are not apparent in the overall statistics. They argue as well that the quality of EPSCoR-funded research is equivalent to other federally funded R&D because awards are based on merit reviews.

270

Energy

Budget function 270 includes funding for the nondefense programs of the Department of Energy as well as for the Tennessee Valley Authority, rural electrification loans, and the Nuclear Regulatory Commission. The programs supported by this function are intended to increase the supply of energy, encourage energy conservation, provide an emergency supply of energy, and regulate energy production. CBO estimates that discretionary outlays for function 270 will be $3 billion in 2000, continuing recent declines in energy spending. Negative balances in mandatory spending for the function result from repayment of loans, receipts from the sale of electricity produced by federal entities, and charges for the disposal of nuclear waste.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	5.6	5.4	5.8	5.8	6.4	6.2	4.9	4.2	3.1	2.9	2.6
Outlays											
Discretionary	4.8	4.4	5.4	5.6	6.4	6.8	6.0	4.9	3.7	3.1	3.0
Mandatory	-1.4	-2.0	-0.9	-1.2	-1.2	-1.8	-3.1	-3.4	-2.4	-2.2	-3.7
Total	3.3	2.4	4.5	4.3	5.2	4.9	2.8	1.5	1.3	0.9	-0.7
Memorandum: Annual Percentage Change in Discretionary Outlays		-7.4	22.4	3.0	15.1	5.7	-11.9	-17.7	-24.4	-15.7	-3.1

270-01 Eliminate the Department of Energy's Applied Research Programs for Fossil Fuels

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	335	134
2002	419	302
2003	419	402
2004	419	419
2005	419	419
2001-2005	2,011	1,676
2001-2010	4,106	3,771
Relative to WIDI		
2001	343	137
2002	437	312
2003	445	421
2004	454	447
2005	463	456
2001-2005	2,142	1,773
2001-2010	4,603	4,195

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

270-02, 270-03, 270-04, and 350-01

The Department of Energy (DOE) currently spends over $400 million annually to improve the applied technologies for finding and using fossil fuels (petroleum, coal, and natural gas). Those programs were put into place when the prices of fossil fuels were controlled and, as a result, incentives for technology development were muted. In a world of deregulation and increasingly free energy markets, the value of federal research and development (R&D) programs in energy is questionable.

One reason for deregulating prices in energy markets is to provide suppliers with incentives to develop newer and better technology and bring it to market. The recent deregulation of electrical generation markets, for example, has already brought a great deal of low-cost generating capacity on line, displacing higher-cost power plants.

In addition, private entities are more attuned to which new technology has commercial promise than are federal officials. Federal programs in the fossil fuel area have a long history of funding technologies that, while interesting technically, had little chance of commercial feasibility, even after years of federal investment. As a result, much of the federal spending has been irrelevant to solving the nation's energy problems.

Critics of the programs argue that DOE should concentrate on basic energy research and reduce the department's involvement in applied technology development. They contend that the federal government has a comparative advantage in developing the basic science for a new energy source but a comparative disadvantage in developing and demonstrating the costly technology. DOE's basic energy science program, critics note, allows university researchers and scientists at the national laboratories to better understand the materials and other sciences underlying energy use.

Finally, because energy prices have been low, potential users of applied technology for new energy sources have had little incentive to invest in implementing it. Consequently, the technology developed by the basic energy science program sometimes sat on the shelf until it became obsolete.

Defenders of the applied research programs argue that federal R&D in those areas helps offset several existing failures in energy markets and that the programs therefore represent a sound investment for the nation. Current energy prices, they argue, do not reflect the environmental damage done by excessive reliance on fossil fuels, including the potential for global warming. In addition, current energy prices do not reflect the military and economic risks posed by reliance on Middle East oil. Although the DOE R&D programs cannot correct market failures in the short term, they may moderate the consequences of such failures over the long term.

270-02 Eliminate the Department of Energy's Applied Research for Energy Conservation

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	461	115
2002	577	398
2003	577	531
2004	577	571
2005	577	577
2001-2005	2,769	2,192
2001-2010	5,654	5,077
Relative to WIDI		
2001	470	118
2002	598	408
2003	609	552
2004	621	603
2005	632	620
2001-2005	2,930	2,301
2001-2010	6,266	5,577

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

270-01, 270-03, 270-04, 270-08, and 350-01

In 2000, the Department of Energy (DOE) will spend $577 million on programs to develop energy conservation technology. Those efforts include the Partnership for the Next Generation Vehicles (discussed in option 270-08) for automobile research as well as industrial and residential energy-efficiency research. Involvement of federal agencies in the selection and development of near-commercial technologies raises questions about the appropriateness of the current division of labor between the public and private sectors in this area.

Opponents of federal spending for energy conservation research and development (R&D) make several arguments. Generally, they argue that the federal government should stay out of applied energy technology development and concentrate on basic research in the science underlying those areas. Specifically, they note that many projects funded through this research effort are small and discrete enough—and, in many cases, have a clear enough market—to warrant private investment. In such instances, DOE may be crowding out or preempting private-sector firms. In other instances, such programs conduct R&D that the intended recipients are likely to ignore—often because it is too expensive or esoteric to implement.

Critics of the programs also note that other federal policies encourage the introduction of some of the technologies. Utilities, for instance, are encouraged to subsidize consumers' purchases of conservation technologies by underwriting the purchase of efficient home appliances. In addition, the tax code favors investments in conservation technology. Thus, federal government R&D programs may be duplicative given such other avenues of support.

Defenders of the programs argue that federal R&D in the energy conservation area helps offset several existing failures in energy markets. Current energy prices, they argue, do not reflect the damage to the environment from excessively relying on fossil fuels, including the potential for global warming. In addition, current energy prices do not reflect the military and economic risks posed by relying on Middle East oil. Although DOE's R&D programs for energy conservation cannot correct market failures in the short term, they can moderate the consequences of those market failures over the long run.

One advantage such programs have had over other DOE R&D efforts in the energy technology area is that many of the individual programs are small. Over the years, many of the best outcomes of the research efforts, such as thin films to make windows more energy efficient, have come from small research investments.

(Because energy conservation R&D and the Partnership for the New Generation Vehicles overlap, the savings from eliminating both programs would be less than the sum of the two options. In addition to its own energy conservation program, DOE separately provides grants to state and local agencies for energy conservation. Those grants are discussed in option 270-04.)

270-03 Eliminate the Department of Energy's Applied Research for Solar and Renewable Energy Sources

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	248	186
2002	310	295
2003	310	310
2004	310	310
2005	310	310
2001-2005	1,488	1,411
2001-2010	3,038	2,961
Relative to WIDI		
2001	253	190
2002	321	304
2003	327	326
2004	333	332
2005	339	338
2001-2005	1,573	1,490
2001-2010	3,364	3,274

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

270-01, 270-02, 350-01, and REV-35

In 2000, the Department of Energy (DOE) will spend $310 million on research and development (R&D) for solar and other renewable energy sources. The largest technology development efforts by far are those for developing alternative liquid fuels from biomass and electricity from photovoltaic cells. Smaller efforts involve electric energy storage and wind energy systems. Phasing out the research would save $1.4 billion over the 2001-2005 time frame.

Opponents of federal support for such research argue that the federal government should stay out of applied energy technology development and concentrate on basic research in the science underlying those areas. Federally sponsored researchers lack the complex market feedback that helps researchers in private companies realize when their technologies become too esoteric or expensive for the market.

Another criticism shared by DOE's conservation R&D programs (discussed in option 270-02) is that many of the research projects funded by the renewable energy program are sufficiently small and discrete and have a clear enough market to attract private funding. (Of course, many of those alternative energies were simply not economical during the long period when oil prices were low.)

The biggest single solar energy program—photovoltaics—has largely succeeded, and program opponents might argue that it may now be time for an orderly withdrawal of federal support. Several large factories are producing photovoltaic cells, mainly for the export market, or are under construction. After nearly three decades of federal support, the market may well be becoming a purely private concern, and the government may wish to withdraw its funding. Foreign firms, critics note, are likely to dominate the market because of their countries' higher domestic energy prices and consequent higher likely demand for alternative energy sources. U.S. consumers may let foreign companies and governments bear the cost of developing the energy sources and then buy the technology when it is cheap and perfected.

For liquid fuels derived from renewable resources, especially biomass, the federal tax code already provides incentives for developing the technology. Ethanol fuels receive special treatment under the federal highway tax (see option REV-35). Furthermore, federal regulations authorized by many different statutes favor alcohol fuels, which now usually mean those that are corn based. Such fuels could be derived from other biomass sources, however, with the right technology.

Defenders of the programs argue that energy markets are still far from perfect. The energy prices consumers pay fail to incorporate both the environmental and national security risks posed by the nation's dependence on fossil fuels. Furthermore, the United States also plays the role of international R&D laboratory for less developed countries, which often have much higher energy costs.

270-04 Eliminate Energy Conservation Grant Programs

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	134	34
2002	168	116
2003	168	155
2004	168	166
2005	168	168
2001-2005	806	639
2001-2010	1,644	1,479
Relative to WIDI		
2001	149	37
2002	174	126
2003	177	163
2004	181	176
2005	184	181
2001-2005	865	683
2001-2010	1,836	1,637

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

270-01, 270-02, 270-03, 300-15, and 600-12

RELATED CBO PUBLICATIONS:

Should the Federal Government Sell Electricity? (Study), November 1997.

Electric Utilities: Deregulation and Stranded Costs (Paper), October 1998.

Weatherization assistance grants supported by the Department of Energy's (DOE's) Office of State and Community Programs help low-income households reduce their energy bills by funding such activities as installing weather stripping, storm windows, and insulation. Institutional conservation grants supported by the office help reduce the use of energy in educational and health care facilities by adding federal funds to private and local public spending to encourage local investment in building improvements. The Office of State and Community Programs also supports the energy conservation programs of states and municipal governments that, for example, establish energy-efficiency standards for buildings and promote public transportation and carpooling. Critics of those programs question whether they actually produce any savings and whether the conservation actions they provide are not already promoted by other programs or laws, such as the Clean Air Act Amendments of 1990. The DOE programs are independent of a similar block-grant activity, the Low Income Home Energy Assistance Program, administered by the Department of Health and Human Services.

This option would halt new appropriations for the block-grant programs that support energy conservation activities by the states. It would save $1.5 billion in outlays from 2001 through 2010.

Arguments supporting this option include diminished concern about energy security, questions about the efficacy of the program, and duplication with other programs or laws. Federal grants to promote less energy consumption reflect the widespread concerns about energy-supply security—for all sources, including oil, natural gas, and coal—prevalent in the mid-1970s. Today, those concerns are more correctly focused on imported oil supplies. State grant programs that help reduce residential and institutional demand for natural gas and coal-generated electricity have little benefit for the cause of oil-supply security. And although the government has urged the reduction of energy use for environmental reasons, federal support for reducing the use of gas and coal through conservation grants for security or environmental needs conflicts with other federal policies that promote the production and use of those fuels.

Proponents of continuing the grant programs claim that eliminating them could impose hardships on states that wish to continue their energy conservation efforts but are financially stressed. Many states still rely heavily on such grants to help low-income households and public institutions. In addition, the voluntary energy savings those programs effect are an important part of the President's Climate Change Action Plan for reducing greenhouse gas emissions. Such considerations may result in continued federal support for the energy conservation grants.

270-05 Eliminate Electrification and Telephone Credit Subsidies Provided by the Rural Utilities Service

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	15	1
2002	15	2
2003	15	6
2004	15	11
2005	15	13
2001-2005	75	33
2001-2010	150	103
Relative to WIDI		
2001	15	1
2002	15	2
2003	16	6
2004	16	11
2005	16	14
2001-2005	78	34
2001-2010	161	111

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

270-06, 270-07, 450-01, REV-42, and REV-43

RELATED CBO PUBLICATIONS:

Should the Federal Government Sell Electricity? (Study), November 1997.

Electric Utilities: Deregulation and Stranded Costs (Paper), October 1998.

The Rural Utilities Service (RUS) is an agency within the Department of Agriculture that, among other activities, offers financial assistance through subsidized loans and grants to electric and telephone companies serving primarily rural areas. Because that purpose has been largely accomplished, questions have arisen as to whether those subsidies should continue to be offered. This option addresses only the credit subsidies provided through loans for electrification and telephone service that were previously administered by the Rural Electrification Administration (REA). The former REA programs were combined with other loan and grant programs in 1994 to form the RUS. (Additional potential savings from cutting other RUS programs are described in option 450-01.)

For 2000, RUS subsidies to electric and telephone companies total about $15 million. In addition, the agency spends nearly $31 million per year administering those programs. Eliminating the credit subsidies for loans made or guaranteed by the RUS would reduce outlays by an estimated $103 million between 2001 and 2010.

The savings shown in the table could result from either of two scenarios: discontinue lending and require RUS borrowers to use private sources of capital for all of their loan needs, or continue a federal loan program but eliminate subsidies. A loan program with no subsidy costs would require raising the interest rates on loans to rural electric and telephone companies to the level of the Treasury's cost of borrowing; it would also mean charging small loan origination fees to cover the cost of defaults for certain classes of loans. In addition to savings in subsidy costs, some savings in administrative costs could result if all such lending was discontinued. Some of the nearly $31 million per year in current salaries and expenses would be required to administer existing loans, but those costs could be gradually reduced under a no-new-lending option. Additional administrative savings over the 2001-2010 period could be achieved by eliminating the program, but those additional savings are not counted in this option.

The loan program for rural electrification and telephone service has largely fulfilled its original goal of making those services available in rural communities. Most of the communities that the RUS subsidizes are now much larger than the original service area requirement of no more than 1,500 inhabitants. RUS borrowers serve about 10 percent of U.S. electricity customers and 4 percent of telephone customers. In addition, more than 95 percent of rural America has electric service. Moreover, most RUS borrowers already use some private financing. Because the cost of interest accounts for only a small percentage of the typical customer's bill, eliminating the remaining federal subsidy would have little effect on the utility rates that most borrowers charge their customers.

Proponents of the RUS claim that many borrowers still depend on federal loans to maintain and expand those utilities. Increasing the interest rates or charging origination fees on some loans would raise the rates that such borrowers charge their customers, especially in the rural regions that are most affected. Borrowers argue that they need some level of subsidization to keep their service and utility rates comparable with those in urban areas.

270-06 Restructure the Power Marketing Administrations to Charge Higher Rates

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	130	130
2003	130	130
2004	130	130
2005	130	130
2001-2005	520	520
2001-2010	1,170	1,170

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

270-05, 270-07, REV-42, and REV-43

RELATED CBO PUBLICATION:

Should the Federal Government Sell Electricity? (Study), November 1997.

The three smallest power marketing administrations (PMAs) of the Department of Energy sell about 1 percent of the nation's electricity: the Western Area Power Administration, the Southwestern Power Administration, and the Southeastern Power Administration. Those PMAs sell power at below-market rates, a practice that some observers find inconsistent with improving the efficiency of energy markets, which is a generally accepted goal of energy policy.

The power generated by the PMAs comes largely from hydropower facilities that the Army Corps of Engineers and the Bureau of Reclamation have built and continue to operate. Current law requires that those sales be made at cost—a situation intended to ultimately reimburse taxpayers for a share of the costs of construction, costs of current operations, and interest on the portion of total costs that has not been repaid. Interest charges are generally below the government's cost of borrowing, which, along with the low cost of generating electricity from hydropower, results in power rates for federal customers that are significantly below the rates that other utilities charge. Current law also requires that PMAs first offer that power to rural electric cooperatives, municipal utilities, and other publicly owned utilities.

Restructuring would require that those three PMAs sell electricity at market rates to any wholesale buyer. Implementing higher rate charges would bring in about $130 million in 2002 and increase total receipts by about $500 million through 2005 relative to the 2000 level.

The rationale for federal power subsidies is not as strong as it once was. The market power of private utilities is checked by federal and state regulation of the power supply, by federal antitrust laws, and, increasingly, by competition from independent power sources. In addition, the disparity between incomes in different regions of the country has diminished. In many cases, neighboring communities—some receiving federal power and some not—have no discernible differences. For households in the regions that the three PMAs serve, federal sales of power meet only a small share of their total power needs; therefore, the impact of increased federal rates on average costs is small. In addition, the prospect of significant future costs of producing electricity from hydropower further supports the case for increasing power rates now. Such costs are for long-deferred maintenance and upgrades and for addressing the environmental needs of threatened species. The opportunity to earn additional revenues from federal power sales may be short-lived: new power sources are becoming increasingly competitive with federal power.

The current beneficiaries of the federal power program believe that restructuring could greatly increase electric utility rates for the many small and rural communities served by PMAs. They also argue that continuing low-cost federal power is necessary to counter the uncompetitive practices of investor-owned utilities and to support the economies of certain regions of the country.

270-07 Sell the Southeastern Power Administration and Related Power Generation Equipment

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	0	0
2003	1,700	1,700
2004	-161	-161
2005	-164	-164
2001-2005	1,375	1,375
2001-2010	511	511

SPENDING CATEGORY:

Mandatory (excludes discretionary savings for operations)

RELATED OPTIONS:

270-05, 270-06, REV-42, and REV-43

RELATED CBO PUBLICATIONS:

Should the Federal Government Sell Electricity? (Study), November 1997.

Electric Utilities: Deregulation and Stranded Costs (Paper), October 1998.

The Southeastern Power Administration (SEPA) of the Department of Energy sells electricity that comes from hydropower facilities that the Army Corps of Engineers has constructed and operates. SEPA pays private transmission companies to deliver that power to over 300 wholesale customers: rural cooperatives, municipal utilities, and other publicly owned utilities. Selling federal power assets would be consistent with the policy goal of increasing efficiency in energy markets.

SEPA power rates are designed to recover for taxpayers a share of the costs of construction, costs of current operations, and a nominal interest charge on the portion of total costs that have not yet been recovered. The average revenues from SEPA power (for sales other than to the Tennessee Valley Authority) are about 2.7 cents per kilowatt-hour (kWh), compared with average revenues in the region of 4.7 cents per kWh.

Selling assets that directly support the production of SEPA electricity would save about $1.4 billion over the 2001-2005 period. That estimate reflects sale proceeds of about $1.7 billion minus a loss of budgetary receipts for that period of about $160 million annually. Those figures do not include discretionary budgetary savings of about $75 million annually from ending appropriations to SEPA and the Corps for operations. The estimate of sale proceeds is based on recent sales of hydroelectric assets in the United States. Corps assets to be transferred would include equipment, such as turbines and generators, but not the dams, reservoirs, or waterside property. The sale would also include rights of access to that equipment and to the water flows necessary for power generation, subject to the constraints of competing uses of water.

The original reasons for establishing SEPA—marketing low-cost power to promote competition and fostering economic development—are no longer compelling to many people because of the small amount of power SEPA sells and because of competitive and regulatory constraints on power rates. Also, selling federal facilities does not mean transferring all water resource functions. The Corps could retain direct responsibility for managing water flows for all uses, including the upkeep of basic physical structures and surrounding properties. Or, as with other nonfederal dams, the terms of the federal license to operate the facility (issued by the Federal Energy Regulatory Commission) could dictate the management of water flows for competing purposes.

Proponents of maintaining federal ownership believe that nonfederal entities lack the proper incentives to perform all of SEPA's functions. Many Corps facilities serve multiple purposes, for example, managing water resources for navigation, flood control, or recreation as well as for power generation. Proponents also argue that increased power rates could accompany selling SEPA. SEPA sales meet only about 1 percent of the total power needs in the 11 states where it operates; however, for a few communities, dependence on SEPA is great.

270-08 Eliminate Federal Funding for the Partnership for New Generation Vehicles

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	187	51
2002	227	153
2003	227	205
2004	227	221
2005	227	223
2001-2005	1,095	853
2001-2010	2,230	1,973
Relative to WIDI		
2001	190	53
2002	234	158
2003	239	212
2004	243	233
2005	247	240
2001-2005	1,153	896
2001-2010	2,450	2,159

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

270-02

The Partnership for New Generation Vehicles (PNGV) is a joint federal/private research effort that performs cooperative, precompetitive automotive research, mainly focusing on energy-efficient vehicles. The program raises the issue of the appropriateness of federal support for commercial technology. The partnership draws on the resources of five federal agencies, most notably the Department of Energy (DOE). Within DOE, the partnership primarily falls under energy conservation, where it received $135 million for 2000. (Because the PNGV and the energy conservation programs—option 270-02—are related, the savings from eliminating both of them would be less than the sum of the two options.)

Critics of the PNGV argue that instead of using general tax revenues to support applied research, the federal government could more fairly increase the efficiency of the nation's automotive fleet by raising gasoline taxes, user fees, or both for vehicles that get low mileage per gallon of fuel. Critics further point out that the program may not reach its goal of creating a production-ready vehicle by 2004. Although the latest National Academy of Sciences evaluation of the program "believes the near-term and long-term technologies the PNGV has focused on have the potential to meet the program's objectives," representatives of the automakers involved in the PNGV have downplayed the prospects for near-term commercialization of the technological advances achieved so far. Competitive pressures also raise doubts about the PNGV's usefulness. Both Honda and Toyota have either begun marketing high-mileage cars in the United States or plan to do so in 2000. If those efforts succeed, then domestic automakers should have sufficient commercial incentive to continue their research and hence should no longer need federal support. Finally, critics contend that because the federal contribution to PNGV has, to date, accounted for only a small fraction of total spending on research and development by participating automakers, those firms could probably finance such efforts privately.

Proponents of the PNGV argue that continuing imperfections in energy markets and environmental considerations make the development of these technologies a public policy matter. Although sports utility vehicles, minivans, and pickups have more than doubled their 1983 market share, claiming 46 percent of the U.S. market in 1999, the PNGV program conducts research that could contribute to the production of high-mileage vehicles. Given the uncertainty surrounding energy prices and environmental issues, levying taxes or user fees to reduce current fuel consumption could impose a burden on consumers that outweighs eventual benefits. From that perspective, federal funding for PNGV is a low-cost option today that will facilitate domestic production of efficient vehicles at a later date. If low-income consumers were more likely to purchase older, inefficient vehicles, research subsidies would then avoid regressive gasoline taxes, user fees, or both.

270-09 Sell Oil from the Strategic Petroleum Reserve

	Savings (Millions of dollars) Budget Authority	Outlays
2001	217	217
2002	266	266
2003	273	273
2004	280	280
2005	287	287
2001-2005	1,323	1,323
2001-2010	1,372	1,372

SPENDING CATEGORY:

Mandatory

RELATED CBO PUBLICATION:

Rethinking Emergency Energy Policy (Study), December 1994.

The Strategic Petroleum Reserve (SPR) is a government-owned stock of crude oil that was first authorized in 1975 to help safeguard the nation against the threat of a severe disruption of oil supplies. The SPR consists of four underground sites along the Gulf of Mexico that together have the capacity to store 680 million barrels of oil. The SPR currently holds about 575 million barrels of oil. The Department of Energy (DOE) can sustain a maximum drawdown of about 4 million barrels per day (20 percent of the nation's current petroleum use) for 90 days. The department has released oil from the SPR in emergency circumstances only once—17 million barrels during the Persian Gulf War. The government's net investment in the SPR is about $16 billion for oil and about $4 billion for storage and transportation facilities. At a price of $20 per barrel, the value of that oil would be about $12 billion.

This option would require DOE to reduce the size and excess capacity of the SPR by closing the smallest storage site, Bayou Choctaw, and selling the site's 68 million barrels of oil over a five-year period. It would place at least 10 million but no more than 20 million barrels on the market each year to minimize the impact of reducing the SPR on world oil prices. The Congressional Budget Office estimates that receipts from the oil sales would total $1.3 billion over the 2001-2005 period, and appropriations for operating the reserve could be reduced after the site is decommissioned toward the end of the decade. The option conforms with past Congressional actions: in 1996 and 1997, the Congress directed DOE to sell SPR oil to offset spending on the SPR and other programs and has authorized DOE to reduce its excess capacity by leasing it to foreign governments or private entities. Thus far, however, efforts to lease excess capacity have not succeeded.

The argument for reducing the SPR is supported by changes in program benefits and costs since 1975. Structural changes in energy markets and the economy at large have reduced the potential cost of disrupting oil supplies and consequently the benefits from releasing oil in a crisis. The increasing diversity of world oil supplies and the growing integration of the economies of oil-producing and oil-consuming nations lessen the risk of such disruptions. Moreover, the experience of DOE in its Persian Gulf War sale and in recent sales indicates that the process of deciding to release oil and the sales mechanism can contribute to market uncertainty, further diminishing the benefits of release. The rising costs of maintaining the SPR also strengthen the case for reducing it: many of the SPR's facilities are aging and have required unanticipated spending for repairs to maintain drawdown capabilities.

Arguments against closing the site and selling the oil stress logistical and pricing concerns. Closing Bayou Choctaw could reduce DOE's flexibility in distributing oil if a drawdown occurred, especially in the Mississippi Valley region. Another argument against this option concerns the effect of selling SPR oil on domestic oil producers, which prompted the Congress to repeal legislation in 1998 requiring oil to be sold.

270-10 Eliminate the Analysis Function of the Energy Information Administration

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	8	5
2002	10	9
2003	10	10
2004	10	10
2005	10	10
2001-2005	48	44
2001-2010	98	94
Relative to WIDI		
2001	8	5
2002	11	10
2003	11	11
2004	11	11
2005	11	11
2001-2005	52	48
2001-2010	114	110

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

350-01

The Energy Information Administration (EIA), created by the Congress in 1977, is an independent statistical agency of the Department of Energy. EIA's mission is to develop data and analyses on energy resources and reserves, production, demand, and technologies as well as related financial and statistical information on the adequacy of energy resources necessary to meet U.S. energy demand. Questions about the appropriateness and current need for those activities underlie this option. Eliminating the analysis function, which includes energy forecasting, would save $5 million in 2001 and reduce outlays by $94 million through 2010 relative to the 2000 funding level.

The Congress created EIA when many people thought that the United States would deplete its reserve of fossil fuels. Because that concern has been alleviated, some argue that eliminating EIA's analysis function is appropriate. Furthermore, some critics of EIA assert that analysis that supports policy decisions is already done by academicians, the Department of Energy's Policy Office, the Congressional Research Service, and the General Accounting Office. In addition, some critics note that industry's willingness to fund specific research activities through trade associations, such as the American Petroleum Institute and the Edison Electric Institute, suggests that EIA is providing a service that the private sector would perform on its own.

EIA supporters claim that an independent party should collect, analyze, and disseminate information. They claim that access to information is important to a competitive market. Although concerns about energy supplies have been alleviated, the Congress is now addressing such issues as global warming. Without independent analysis, the Congress would have to choose among conflicting analyses done by the Administration, environmental groups, and industry sources.

Additional savings could be obtained by eliminating some of EIA's data collection or moving EIA's data collection responsibilities to other agencies such as the Federal Energy Regulatory Commission. Much of the information collected and distributed by the EIA is available through newspapers and trade sources. Natural gas and electricity futures prices are traded on the New York Mercantile Exchange, among others, and are published daily in the *Wall Street Journal*. Although EIA conducts its own statistical surveys, it also develops reports based on information collected by the Federal Energy Regulatory Commission.

270-11 Require the Tennessee Valley Authority to Accelerate the Repayment of Deferred Nuclear Assets and Limit Its Future Borrowing

	Outlay Savings (Millions of dollars)
2001	0
2002	275
2003	275
2004	275
2005	275
2001-2005	1,100
2001-2010	2,475

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

270-05, 270-06, 270-07, REV-42, and REV-43

RELATED CBO PUBLICATION:

Should the Federal Government Sell Electricity? (Study), November 1997.

The Tennessee Valley Authority (TVA), a federal agency, is one of the largest electric utilities in the nation. Under current law, TVA sets rates for the electricity that it sells so that over time, receipts from its sales will be sufficient to pay for the program's routine operations, capital projects, and certain nonpower activities. TVA finances some of those costs by borrowing from the public, subject to a limit of $30 billion on the amount of its outstanding debt at any given time. Currently, TVA's outstanding debt totals about $26 billion, an amount that the agency and others suggest may be too high in today's increasingly competitive electricity market. Of particular concern is the agency's ability to repay $6.3 billion that it has invested in building nuclear power plants whose completion has been deferred.

This option would amend laws governing TVA's financial operations in two ways. First, it would require the agency to pay off its $6.3 billion investment in deferred nuclear assets within the next 10 years. (Those payments would be in addition to the agency's regular depreciation of its other assets.) Second, the option would lower the limit on TVA's outstanding debt to $26 billion for fiscal year 2001 and periodically reduce that limit further so that the borrowing cap equals $18 billion by the end of 2010. The Congressional Budget Office estimates that those changes would reduce TVA's net outlays by an average of about $275 million a year beginning in 2002. Savings over the 2001-2005 period would total about $1.1 billion.

In addition to those savings, CBO expects TVA to retire substantial amounts of its debt under current law. In 1997, the agency announced a series of actions aimed at cutting its debt in half by 2007. Despite those initiatives, however, TVA has paid off less debt over the past two years than it planned, largely because of additional spending on new power plants and emission controls. CBO projects that under current law, TVA's outstanding debt will decline to about $20.5 billion by the end of 2010. The savings from this option could result from reductions in spending, increases in power revenues, or some combination of the two.

This option would address several concerns about TVA operations. Adopting a statutory timetable for repaying TVA's investment in deferred assets would allay concerns about taxpayers—rather than the TVA system—being saddled with those costs if TVA has to reduce its prices in the future to stay competitive. Indeed, a key rationale for reducing TVA's debt-related costs is to increase the agency's flexibility in setting rates so that it can remain a viable competitor in the future. Lowering the debt limit would bring the statutory ceiling in line with TVA's long-term plans, giving customers greater assurance that debt-related costs could not climb in the future unless authorized by the Congress.

Advocates for the status quo argue that such restrictions are unnecessary and could impair TVA's ability to manage its $6-billion-a-year electricity business efficiently. They point to the initiatives that the agency announced in 1997 as evidence that market forces, rather than new government controls, will lead TVA to lower its debt and restrain its spending. They also argue that this option could force TVA to keep prices higher than anticipated, at least in the near term.

300

Natural Resources and Environment

Budget function 300 supports programs administered by the Army Corps of Engineers, the Department of Agriculture, the Department of the Interior, the Environmental Protection Agency, and the Department of Commerce's National Oceanic and Atmospheric Administration. Those programs involve water resources, conservation, land management, pollution control, and natural resources. CBO estimates that discretionary outlays for function 300 will total $23.8 billion in 2000. Over the past decade, spending under this function has increased almost every year.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	18.6	19.6	21.3	21.4	22.4	20.4	20.6	22.4	23.4	23.8	24.1
Outlays											
Discretionary	17.8	18.6	20.0	20.1	20.8	21.9	20.9	21.3	21.9	23.7	23.8
Mandatory	-0.7	0	0	0.2	0.2	0	0.6	-0.1	0.4	0.3	0.7
Total	17.1	18.6	20.0	20.2	21.0	21.9	21.5	21.2	22.3	24.0	24.5
Memorandum:											
Annual Percentage Change in Discretionary Outlays		4.5	7.7	0.2	3.7	5.4	-4.6	1.7	3.0	7.9	0.5

300-01 Increase Net Receipts from National Timber Sales

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	50	45
2002	65	60
2003	85	80
2004	105	95
2005	120	115
2001-2005	425	395
2001-2010	1,050	1,010
Relative to WIDI		
2001	50	45
2002	70	65
2003	90	85
2004	120	110
2005	140	135
2001-2005	470	440
2001-2010	1,230	1,190

SPENDING CATEGORY:

The net of reduced discretionary outlays and forgone mandatory receipts.

RELATED OPTIONS:

300-01, 300-06, 300-07, and 300-08

The Forest Service (FS) manages federal timber sales from 119 national forests. The spending necessary to make those sales in some cases is larger than the receipts paid to the government. As a result, questions have arisen about whether those sales should be made.

In fiscal year 1997, the FS sold roughly 3.7 billion board feet of public timber. Purchasers may harvest the timber over several years and pay the FS upon harvest. The total fiscal year 1997 harvest, approximately 3.3 billion board feet, represented a continuing decline in volume from previous years. According to *Timber Sales Program Annual Reports* published by the FS, in fiscal years 1996 and 1997, the FS spent more on the timber program than it collected from companies harvesting the timber. In 1997, the timber expenses reported by the FS exceeded timber receipts by about $90 million. The annual reports exclude receipt-sharing payments to states from the calculation of timber expenses. When such payments are included, timber expenses exceeded receipts by more than $160 million (or almost 30 percent) in fiscal year 1997.

The FS does not maintain the data needed to estimate annual timber receipts and the expenditures associated with each individual timber sale. Therefore, it is hard to determine precisely the possible budgetary savings from phasing out all timber sales in the National Forest System for which expenditures are likely to exceed receipts. To illustrate the potential savings, however, this option estimates the reduction in net outlays in the federal budget from eliminating all future timber sales in five National Forest System regions for which imbalances between cash receipts and expenditures were prominent in fiscal years 1996 and 1997.

In those five regions (the Northern, Rocky Mountain, Southwestern, Intermountain, and Alaska regions), cash expenditures exceeded cash receipts by at least 30 percent in 1996 and 1997. Eliminating all future timber sales from those regions would reduce the FS's outlays for the 2001-2010 period by about $1,570 million; timber receipts (which are categorized as mandatory) would fall by about $560 million after subtracting payments to states, producing net savings of $1,010 million. (Hence, the savings estimates are the net effect of changes in both discretionary and mandatory budgets.)

Timber sales for which spending exceeds receipts have several potential drawbacks. They may lead to reductions in the federal surplus, excessive depletion of federal timber resources, and destruction of roadless forests that have recreational value.

Potential advantages of the sales include community stability in areas dependent on federal timber for logging and other related jobs. Timber sales also improve access to the land—as a result of road construction—for fire protection and recreation.

300-02 Impose a Ten-Year Moratorium on Land Purchases by the Departments of Agriculture and the Interior

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	457	185
2002	457	332
2003	457	430
2004	457	465
2005	457	457
2001-2005	2,285	1,869
2001-2010	4,570	4,154
Relative to WIDI		
2001	464	186
2002	474	334
2003	482	437
2004	491	480
2005	498	489
2001-2005	2,409	1,926
2001-2010	5,048	4,517

SPENDING CATEGORY:

Discretionary

For 2000, the Departments of Agriculture and the Interior have received appropriations of about $467 million to buy land that is generally used to create or expand designated recreation and conservation areas, including national parks, national forests, wilderness areas, and national wildlife refuges. This option proposes placing a 10-year moratorium on future appropriations for land acquisition by those departments. It would provide for a small annual appropriation ($10 million) to cover emergency acquisition of important tracts that became available on short notice, compensation to "inholders" (landholders whose property lies wholly within the boundaries of an area set aside for public purposes, such as a national park), and ongoing administrative expenses. Savings from this option would total $4.2 billion through 2010.

Proponents of this option argue that land management agencies should improve their stewardship of the lands they already own before taking on additional management responsibilities. In many instances, the National Park Service, the Forest Service, and the Bureau of Land Management find it difficult to maintain and finance operations on their existing landholdings. Furthermore, given the limited operating funds of those agencies, environmental objectives such as habitat protection and access to recreation might be best met by improving management in currently held areas rather than providing minimal management over a larger domain. Supporters of this option also argue that the federal government already owns enough land. Currently, about 650 million acres—approximately 30 percent of the United States' land mass—belong to the government, according to the General Services Administration. The sentiment that that amount is sufficient is particularly strong in the West, where the government owns about 62 percent of the land area in 11 states.

Opponents of this option argue that future land purchases are necessary to achieve ecosystem management objectives and fulfill existing obligations for national parks. Much of the land targeted by the Congress for new and expanded federal reserves is privately held, and acquiring it will require purchases. Furthermore, encroaching urban development and related activities outside the boundaries of national parks and other federal landholdings may be damaging the federal resources. Land acquisition is an important tool for mitigating that problem. Acquisitions that consolidate landholdings may also help improve the efficiency of public land management.

300-03 Eliminate Federal Grants for Water Infrastructure

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	2,582	129
2002	2,582	516
2003	2,582	1,291
2004	2,582	2,066
2005	2,582	2,453
2001-2005	12,910	6,455
2001-2010	25,820	18,720
Relative to WIDI		
2001	2,582	129
2002	2,626	519
2003	2,668	1,302
2004	2,714	2,098
2005	2,760	2,521
2001-2005	13,350	6,569
2001-2010	27,865	19,822

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

450-01

RELATED CBO PUBLICATION:

The Economic Effects of Federal Spending on Infrastructure and Other Investments (Paper), June 1998.

The Clean Water Act (CWA) and the Safe Drinking Water Act (SDWA) require municipal wastewater and drinking water systems to meet certain performance standards to protect the quality of the nation's waters and the safety of its drinking water supply. The CWA provides financial assistance so communities can construct wastewater treatment plants that comply with the act's provisions. The 1996 amendments to the SDWA authorized a state revolving loan program for drinking water infrastructure. For 2000, the Congress appropriated about $2.6 billion for water infrastructure programs, including funds for wastewater programs and the relatively new program for drinking water facilities. Ending all funding of new water infrastructure projects after 2000 would save $18.7 billion through 2010 measured against the 2000 funding level.

Title II of the CWA provides for grants to states and municipalities for constructing wastewater treatment facilities. As amended in 1987, the CWA phased out title II grants and authorized a new grant program under title VI to support state revolving funds (SRFs) for water pollution control. Under the new system, states continue to receive federal grants, but now they are responsible for developing and operating their own programs. For each dollar of title VI grant money a state receives, it must contribute 20 cents to its SRF. States use the combined funds to make low-interest loans to communities for building or upgrading municipal wastewater treatment facilities. Although authorization for the SRF program under the CWA has expired, the Congress continues to provide annual grant appropriations.

As amended in 1996, the SDWA authorizes the Environmental Protection Agency to make grants to states for capitalizing revolving loan funds for treating drinking water. As with the CWA's wastewater SRF program, states may use those funds to make low-cost financing available to public water systems for constructing facilities to treat drinking water. In 2000, the Congress appropriated $820 million for capitalization grants for drinking water SRFs.

Proponents of eliminating federal grants to water-related SRFs say such grants may encourage inefficient decisions about water treatment by allowing states to loan money at below-market interest rates. Below-market loan rates could reduce incentives for local governments to find less costly alternatives for controlling water pollution and treating drinking water. In addition, federal contributions to wastewater SRFs were intended to help move toward full state and local financing of the funds by 1995. Thus, proponents of ending federal grants to those SRFs argue that the program was intended to be temporary and may have replaced, rather than supplemented, state and local spending.

Opponents of such cuts argue that states and localities could have trouble meeting the federal treatment deadlines without continued federal support—both because repayments to the SRFs would be too small to fund new projects and because states would be unable to handle the additional cost of offsetting decreased federal contributions.

Opponents of the cuts also have concerns about helping small and economically disadvantaged communities that have had the most difficulty complying with CWA and SDWA requirements. Some people who oppose eliminating the federal grants maintain that doing so would increase the burden of unfunded federal mandates on state and local governments.

300-04 Spend the Remaining Balance of the Superfund Trust Fund and Terminate the Program

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	0	0
2002	1,400	350
2003	1,400	840
2004	1,400	1,120
2005	1,400	1,260
2001-2005	5,600	3,570
2001-2010	12,600	10,220
Relative to WIDI		
2001	0	0
2002	1,461	365
2003	1,493	885
2004	1,524	1,196
2005	1,555	1,367
2001-2005	6,033	3,813
2001-2010	14,314	11,469

SPENDING CATEGORY:

Discretionary

Since 1981, the Superfund program of the Environmental Protection Agency (EPA) has been charged with cleaning up the nation's worst hazardous waste sites, particularly those on the National Priorities List (NPL). The program made progress in the 1990s, especially in increasing the number of sites in the final phase of the cleanup process, but more work remains. As of the end of fiscal year 1999, EPA had identified 670 of 1,403 NPL sites addressed through the Superfund program as "construction complete," meaning that all physical construction work required for the cleanup effort (capping a landfill, installing a groundwater treatment system, and the like) was done. Conversely, remedy construction had begun but had not been completed at 438 current NPL sites and had not yet started at 304 sites. In addition, EPA has proposed that another 58 sites be added to the list, and hundreds more sites with NPL-caliber problems probably remain to be identified.

Although the Congress could choose to end the program at any time, one notable occasion to do so might be the forthcoming depletion of the Hazardous Substance Superfund, the trust fund that has been the main source of the program's appropriations. The trust fund balance has declined since Superfund's "environmental income tax" on corporations and excise taxes on oil, petroleum products, and certain chemicals expired in 1995. The trust fund is projected to end fiscal year 2000 with an unappropriated balance of roughly $1.1 billion, more than enough for fiscal year 2001 given current levels of spending and appropriations from the general fund. If the end of 2001 is too close at hand to allow a safe and orderly program shutdown, the Congress could reduce annual spending to stretch the same total funding for additional months or years.

The argument for spending the trust fund balance and terminating the program asserts that Superfund efforts are not worthwhile, at least not at the federal level. Superfund's critics argue that the program's cost is disproportionate to the threat represented by hazardous waste sites and that its system of retroactive, joint-and-several liability is irremediably inefficient and unfair. They also argue that waste sites are local problems that are more appropriately handled by the states, almost all of which have their own hazardous waste cleanup programs for sites not addressed under federal law. In addition, although depleting the trust fund has no budgetary significance, it provides a near-term opportunity to shut the program down—unlike, for example, merely closing the NPL to new sites, which would require maintaining some federal program for most or all of the decade.

Superfund's defenders point to evidence linking Superfund sites to human health problems, including birth defects, leukemia, cardiovascular abnormalities, respiratory illnesses, and immune disorders, and note that the public places a high priority on waste cleanup. They argue further that Superfund has reduced costs and completed more cleanups in recent years and that modest legislative reforms can improve the program. Finally, they note that states vary widely in their capacity to handle NPL-caliber problems.

300-05 Charge Market Rates for Information Provided by the National Weather Service

	Added Receipts (Millions of dollars)
2001	2
2002	2
2003	2
2004	2
2005	2
2001-2005	10
2001-2010	20

SPENDING CATEGORY:

This fee could be classified as a discretionary offsetting collection or a mandatory offsetting receipt depending on the specific language of the legislation establishing the fee.

RELATED OPTIONS:

370-02 and 400-05

The National Weather Service (NWS) provides public forecasts, weather and flood warnings, and severe-weather advisories to protect lives and reduce property damage from those hazards. The annual budget for such services, including operating weather satellites, is about $1 billion. Currently, the NWS allows open access to all of its weather data and information services. Commercial users—such as the Weather Channel and Accu-Weather—pay fees only for the costs of computer hookups and transmission of NWS data. Moreover, the NWS charges nothing for information received from its satellite broadcasts or Internet site. Charging fees that are based on the fair market value of access to that information, except for severe-weather warnings, could raise $2 million in 2001, $10 million over five years, and $20 million over 10 years.

Charging market value for general weather information might lessen its dissemination but encourage the production and presentation of more useful information. Supporters of this option contend that charging market-based fees would not substantially reduce the public's access to weather reports. For example, as long as the news media will pay for private forecasts, the market will demand NWS products. In addition, because the fees would not apply to severe-weather warnings, the safety of the general public would not be compromised. Many European nations routinely charge users for weather information provided by their satellites. For example, the British Meteorological Office raises over $30 million a year from commercial customers.

In the past, the NWS viewed charging fair market fees as a significant barrier to the public's access to its information. The Omnibus Budget Reconciliation Act of 1990 attempted to set fees based on the fair market value of NWS data and information, except for information related to warnings and watches, information provided under international agreements, and data for nonprofit institutions. However, the NWS received approval from the Office of Management and Budget to reset the user fee to recover only the cost of disseminating the information.

300-06 Change the Revenue-Sharing Formula from a Gross-Receipt to a Net-Receipt Basis for Commercial Activities on Federal Lands

	Savings (Millions of dollars) Budget Authority	Outlays
2001	185	185
2002	185	185
2003	190	190
2004	190	190
2005	190	190
2001-2005	940	940
2001-2010	1,935	1,935

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

300-01, 300-07, and 300-08

The federal government owns about 650 million acres of public lands—nearly one-third of the United States' land mass. Those lands contain a rich supply of natural resources: timber, coal, forage for livestock, oil and natural gas, and many nonfuel minerals. Private interests have access to much of the federal land to develop its resources and generally pay fees to the federal government depending on the commercial returns realized. In many cases, the federal government allots a percentage of those receipts to the states and counties containing the resources, as compensation for tax revenues they did not receive from the federal lands within their boundaries. The federal government typically calculates those allotments on a gross-receipt basis before accounting for its program costs. The practice sometimes causes the federal government's costs to exceed its share of receipts. Shifting payments to a net basis would reduce federal outlays.

In most cases, the Forest Service is required to allot 25 percent of its gross receipts from commercial activities in the national forests to the respective states and counties. The Department of the Interior allots 4 percent of its timber receipts, an average of 18 percent of its grazing fees, and 4 percent of its mining fees from "common variety" materials to the states; the department's Minerals Management Service (MMS) allots 50 percent of its adjusted onshore oil, gas, and other mineral receipts to the states. The MMS deducts 50 percent of its administrative costs from the gross-receipt calculation before distributing those payments. In effect, the states share 25 percent of the burden of those administrative costs. On certain federal lands—specifically, national forests affected by protection of the spotted owl and the Oregon and California grant lands—payments to states and counties are guaranteed on the basis of an average of past payments. (Such guaranteed payments expire after 2003. This option assumes that administrative costs would be deducted from the guaranteed payments on the basis of past receipts and from other state payments on the basis of current receipts.)

Federal savings would be substantial if the Congress required those agencies to deduct their full program costs from gross receipts before paying the states. The regional jurisdictions would continue to receive the same allotted percentage of net federal receipts and accrue receipt shares totaling about $710 million in 2001. The projected savings do not include potential federal cost increases under the Payment in Lieu of Taxes (PILT) program, which was established to offset the effects of nontaxable federal lands on local governments' budgets. Payments in lieu of taxes are partially reduced by the amount of revenue-sharing payments from federal agencies. Payments under the PILT program would increase by about $30 million a year beginning in fiscal year 2001 if net program receipts were shared and the Congress appropriated such an increase.

Changing the revenue-sharing formula to a net-receipt basis would probably cause economic hardship to the respective states and counties, greatly reducing their revenue. That might lead to severe cuts in state and county spending. To help alleviate that hardship, the formula could switch gradually to the net-receipt basis over several years.

300-07 Reauthorize Holding Fees and Charge Royalties for Hardrock Mining on Federal Lands

	Added Receipts (Millions of dollars)
2001	36
2002	44
2003	41
2004	41
2005	41
2001-2005	203
2001-2010	408

SPENDING CATEGORY:

This fee could be classified as a discretionary offsetting collection or a mandatory offsetting receipt depending on the specific language of the legislation establishing the fee.

RELATED OPTIONS:

300-01, 300-06, 300-08, and 300-11

RELATED CBO PUBLICATIONS:

Review of the American Mining Congress Study of Changes to the Mining Law of 1872 (Memorandum), April 1992.

Alternative Proposals for Royalties on Hardrock Minerals (Testimony), May 1993.

The General Mining Law of 1872, which originally supported an overall policy of encouraging settlement of the American West, governs access to hardrock minerals—including gold, silver, copper, and uranium—on public lands. Unlike producers of fossil fuels and other minerals from public lands, miners do not pay royalties to the government on the value of hardrock minerals. Instead, under the above law, any holder of more than 10 mining claims on public lands must pay an annual holding fee of $100 per claim, and all claimholders must pay a $25 location fee when recording a claim. However, authorization to collect the holding and location fees expires in 2000.

Estimates place the current gross value of hardrock minerals production at about $650 million annually (excluding claims with so-called first-half patents). That sum has diminished greatly in recent years because of patenting activity. (In patenting, miners gain title to public lands by paying a one-time fee of $2.50 or $5.00 an acre.) This option would reauthorize the current holding fee and location fee and assumes that such fees would be recorded as offsetting receipts to the Treasury. (They are currently counted as offsetting collections to appropriations.) The option also considers an 8 percent royalty that the Congress could impose on the production of hardrock minerals from public lands. The royalty would be on net proceeds (defined here as sales revenues minus costs that include mining, separation, transportation, and other items).

Total budgetary savings from those action would be $408 million over the 2001-2010 period. Of that total, reauthorization of holding and location fees account for about $330 million and royalty collections for about $78 million. Those estimates assume that states in which the mining takes place receive 25 percent of the gross royalty receipts. They also assume that no further patenting of public lands occurs. (In comparison, royalties based on gross proceeds would raise more. In general, the costs of administering any royalty based on net proceeds would exceed those for a royalty based on gross proceeds.)

People in favor of reforming mining law—including many in the environmental community—argue that low holding fees and zero royalties make it less costly to produce on federal lands than on private lands (where payment of royalties is the rule). That policy encourages overdevelopment of public lands, which may cause severe environmental damage. Reforming the law could promote other uses of those lands, such as recreation and wilderness conservation.

Opponents of reform argue that without free access to public resources, exploration for hardrock minerals in this country—especially by small miners —would decline. They also argue that royalties would diminish the profitability of many mines, leading to scaled-back operations or closure and adverse economic consequences for mining communities in the West. Because many mineral prices are set in world markets, miners would be unable to pass along new royalty costs to consumers.

300-08 Raise Grazing Fees on Public Lands

	Added Receipts (Millions of dollars)
2001	2
2002	4
2003	5
2004	7
2005	8
2001-2005	26
2001-2010	84

SPENDING CATEGORY:

This fee could be classified as a discretionary offsetting collection or a mandatory offsetting receipt depending on the specific language of the legislation establishing the fee.

RELATED OPTIONS:

300-01, 300-06, and 300-07

The federal government owns and manages about 650 million acres of U.S. land. The land has many purposes, including grazing of privately owned livestock. Cattle owners compensate the government for using the land by paying grazing fees; the fees, however, may not give the public a fair return.

The Forest Service and the Bureau of Land Management (BLM) administer livestock grazing on public rangelands in the West. In 1998, ranchers were authorized to use about 15 million animal unit months (AUMs)—a standard measure of forage—for grazing on those lands. In 1990, the appraised value of public rangeland in six Western states varied between $5 and $10 per AUM. A 1993 study indicated that the Forest Service and BLM spent $4.60 per AUM in that year to manage their rangelands for grazing. The 1993 permit fee, however, was $1.86 per AUM. Thus, the current fee structure may subsidize ranchers. (The current fee is $1.35 per AUM.)

The Public Rangelands Improvement Act of 1978 established the current formula for grazing fees. It uses a 1966 base value of $1.23 per AUM and makes adjustments to account for changes in beef cattle markets and production input markets. The Congress has considered various proposals to increase grazing fees. The increase in federal receipts resulting from any such proposal depends on the degree to which ranchers reduce their use of AUMs in response to higher fees. One proposal is to allocate grazing rights through a bidding process as long as competition is not too limited. Another option is to follow the states' lead. The federal government would determine grazing fees for federal lands in each state the same way the particular state determines grazing fees on state-owned lands. The government would implement this proposal over 10 years as existing permits expired. The 10-year savings estimate of $84 million is net of additional payments to states of about $22 million. It does not include any additional appropriations for range improvements that could result from added receipts.

Proponents of this option believe that low fees that subsidize ranching contribute to overgrazing and deteriorated range conditions. They support the approach of following decisions made at the state level and reject the one-size-fits-all nature of the current federal fee. State grazing fees and the means of calculating them vary widely by state and sometimes even within a state. Supporters of this approach also point out that states' interest in the revenue received from both state and federal fees lessens any incentive to manipulate state fees to lower federal fees.

Opponents of this approach note that state rangelands may be more valuable than federal lands for grazing purposes. Some systems used by states to establish fees may not reflect those differences in land quality and conditions of use when applied to federal lands. For example, that concern does not exist in states using auction or appraisal systems for setting fees. People in states using fee formulas, however, have that concern. Opponents also point out that the administrative costs of using different procedures to establish federal grazing fees in each state will be higher than those incurred under the current uniform federal fee structure. (This option does not consider possible differences in administrative costs.)

300-09 Recover Costs Associated with Administering the U.S. Army Corps of Engineers Permitting Programs

	Added Receipts (Millions of dollars)
2001	9
2002	19
2003	19
2004	19
2005	19
2001-2005	85
2001-2010	180

SPENDING CATEGORY:

This fee could be classified as a discretionary offsetting collection or a mandatory offsetting receipt depending on the specific language of the legislation establishing the fee.

RELATED OPTIONS:

300-12, 400-04, and 400-05

RELATED CBO PUBLICATION:

Regulatory Takings and Proposals for Change (Study), December 1998.

The Department of the Army, through the U.S. Army Corps of Engineers, administers laws pertaining to the regulation of U.S. navigable waters, including wetlands. Section 404 of the Clean Water Act (CWA) requires that any private, commercial, or government actor desiring to dredge or place fill material in U.S. waters or wetlands must obtain a permit from the Corps. By increasing permit fees, the Corps could recover a portion of its annual regulatory costs. Imposing one type of fee structure for section 404 permitting—a cost-of-service fee on commercial applicants—would generate $9 million in 2001 and a total of $180 million through 2010.

From rather inauspicious beginnings, section 404 of CWA has grown to become the core of the nation's effort to protect wetlands. As legally interpreted, the terms "dredge" and "fill" encompass virtually any activity on a wetland in which dirt is moved, effectively granting the Corps permitting jurisdiction over all wetlands, including those not associated with traditionally navigable waterways. In fiscal year 2000, the Corps's regulatory program budget is $117 million, which mainly funds permitting activities. In fiscal year 1996 (the most recent year for which data are available), the Corps received about 65,000 applications for section 404 permits for discharging dredged or fill materials. Under section 404, the Corps is required to evaluate each permit application and grant approval or denial on the basis of expert opinion and statutory guidelines. The bulk of the permits are quickly approved through outstanding general or regional permits, which grant authority for many low-impact activities. Evaluation of permits not covered by outstanding permits may require the Corps to conduct detailed, lengthy, and costly reviews.

Currently, fees levied for commercial and private permits are $100 and $10, respectively. Government applicants do not pay a fee. The fee structure has not changed since 1977. Total fee collections fall far short of covering the costs of administering the permitting program, particularly for applications requiring detailed review. The Administration has proposed changing the permit fee structure: its Wetland Plan would increase permit fees for commercial projects and eliminate the fees for private, noncommercial projects.

Proponents of higher fees argue that parties pursuing a permit should bear the cost of the permit—not the general taxpaying public. Since permit seekers are advancing a private interest whose benefits accrue to a private party, the costs should be borne by that party. Taxpayers should not have to pay for something that advances the interests of a comparative few.

Permit seekers oppose such fees because they do not want to fund something that may ultimately deny them the right to use their land in the way they choose. The goal of the section 404 permitting program is to advance a public interest by protecting wetlands. Since society benefits from wetlands protection, often at the perceived expense of property owners, society should pay. Furthermore, the regulatory process that property owners must navigate is already onerous, and raising the permit fees would add yet another cost, further infringing on property owners' rights.

300-10 Impose User Fees on the Inland Waterway System

	Added Receipts (Millions of dollars)
2001	0
2002	233
2003	467
2004	467
2005	467
2001-2005	1,634
2001-2010	3,969

CATEGORY:

This fee could be classified as a discretionary offsetting collection, a mandatory offsetting receipt, or a tax receipt, depending on the specific language of the legislation establishing the fee.

RELATED OPTIONS:

300-12, 400-04, 400-05, and 400-06

RELATED CBO PUBLICATION:

Paying for Highways, Airways, and Waterways: How Can Users Be Charged? (Study), May 1992.

The Congressional Budget Office estimates that the Army Corps of Engineers annually spends about $640 million for the nation's inland waterway system. Of that total, about $470 million is for operation and maintenance (O&M), and about $170 million is for new construction. Current law allows up to 50 percent of new inland waterway construction to be funded by revenues from the inland waterway fuel tax, a levy on the fuel consumed by tow boats using most segments of the inland waterway system. All O&M expenditures are paid by general tax revenues.

Imposing user fees high enough to recover fully both O&M and construction outlays for inland waterways would save about $1.6 billion during the 2001-2005 period and about $4 billion over 10 years. The receipts could be considered tax revenues, offsetting receipts, or offsetting collections, depending on the form of the implementing legislation. Receipts could be increased by raising fuel taxes, imposing charges for the use of locks, or imposing fees based on the weight of shipments and distance traveled. The estimates do not take into account any resulting reductions in income tax revenues.

Imposing higher fees on users of the inland waterway system could improve the efficiency of its use by forcing shippers to choose the most efficient transportation route rather than the most heavily subsidized one. Moreover, user fees would encourage more efficient use of existing waterways, reducing the need for new construction to alleviate congestion. Finally, user fees send market signals that identify the additional projects likely to provide the greatest net benefits to society.

The effects of user fees on efficiency would depend largely on whether the fees were set at the same rate for all segments of a waterway or on the basis of the cost of each segment. Since costs vary dramatically by segment, systemwide fees would offer weaker incentives for cost-effective spending because they would cause users of segments with low costs per ton-mile to subsidize users of high-cost segments. Fees based on the cost of each segment, by contrast, could cause users to abandon high-cost segments of the waterways.

One argument against user fees is that they may repress regional economic development. Imposing higher user fees would also lower the income of barge operators and grain producers in some regions, but those losses would be small in the context of overall regional economies.

300-11 Open the Coastal Plain of the Arctic National Wildlife Refuge to Leasing

	Added Receipts (Millions of dollars)
2001	0
2002	0
2003	0
2004	0
2005	1,150
2001-2005	1,150
2001-2010	1,155

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

300-07 and 300-08

The Arctic National Wildlife Refuge (ANWR) consists of 19 million acres in northeastern Alaska, of which 1.5 million acres are coastal plain. The coastal plain is the yet-to-be-explored onshore area with perhaps the country's most promising oil production potential. It is also the least disturbed Arctic coastal region—valued for species conservation and subsistence use.

ANWR was established by the Alaska National Interest Lands Conservation Act of 1980. The refuge serves to conserve fish and wildlife habitats, fulfill related international treaty obligations, provide opportunities to continue indigenous lifestyles, and protect water quality. The act prohibits industry activity in ANWR unless specifically authorized by the Congress.

This option would open ANWR's coastal plain to leasing and development. Leasing would be likely to result in bonus bid payments, ongoing rental payments, and (once production begins, up to 10 or more years after leasing) royalties. As in recent proposals, the Congressional Budget Office assumes the federal government would receive one-half of the offsetting receipts from those sources; the state of Alaska would receive the other half.

The Department of the Interior's most recent assessment of the area's economically recoverable undiscovered petroleum resources is expressed in probabilities and assumptions about the price of oil at the time of production. For this estimate, CBO assumed an average price of $18 per barrel (in 1996 dollars) during the 2010-2030 period, partly on the basis of the Energy Information Administration's price forecast for 2020. At $18 per barrel (delivered to the West Coast), the Department of the Interior estimates a 50 percent probability that at least 2.4 billion barrels of oil will be produced. Using that mean resource assessment and assuming that ANWR lease sales are held within the next 10 years, CBO estimates that leasing ANWR would generate about $2.3 billion from bonus bids over the 2001-2010 period (with half of that amount going to Alaska). Conversely, if oil prices were to grow only at the rate of inflation after 2010, the Department of the Interior's mean resource assessment indicates that no oil would be economically recoverable from ANWR. At an expected price of $15 per barrel, leasing might not generate any significant proceeds for the government.

Arguments in favor of this option include the national security advantages of reducing dependence on imported oil. Most of ANWR would remain closed to development, and the part of the coastal plain that would be directly affected by oil drilling and production represents less than 1 percent of ANWR. Moreover, technological changes in the industry have improved its ability to safeguard the environment.

Arguments against this option include the short-term nature of the still uncertain gain from extracting a nonrenewable resource: it will not provide lasting energy security. The coastal plain is ANWR's most biologically productive area and sustains the biological productivity of the entire refuge. Industrial activity poses a threat to wildlife and the environment despite efforts to mitigate its impact.

300-12 Impose a New Harbor Maintenance Fee

	Added Receipts (Millions of dollars)
2001	164
2002	281
2003	233
2004	180
2005	124
2001-2005	982
2001-2010	612

NOTE: Figures are net of revenues lost from repealing the existing harbor tax.

SPENDING CATEGORY:

This fee could be classified as a discretionary offsetting collection or a mandatory offsetting receipt depending on the specific language of the legislation establishing the fee.

RELATED OPTIONS:

300-09, 300-10, 400-04, and 400-05

On March 31, 1998, the Supreme Court found that the harbor maintenance tax (as it applied to exports) violated the constitutional restriction that "No tax or duty shall be laid on articles exported from any State." Collection of the tax as applied to exports ceased on April 25, 1998. One way to replace the revenue formerly generated by the harbor maintenance tax is to develop a new system of harbor fees that is constitutional. Under such a system, the commercial users of U.S. ports would pay a fee based on port use rather than a payment based on cargo value. Such fees would apply to imports, exports, and domestic shipments. Taxes currently levied on imports and domestic shipments would be rescinded. Moneys generated by the fee would help support harbor operation, construction, and maintenance. The Administration has proposed such a program.

The Army Corps of Engineers now spends about $960 million annually for costs associated with operating, constructing, and maintaining commercial ports nationwide. A major part of those activities is maintaining adequate channel depths. Replacing what remains of the harbor maintenance tax with a more comprehensive fee on commercial port users would generate $164 million in 2001, $281 million in 2002, and $982 million over the 2001-2005 period.

Two arguments can be made for imposing a harbor maintenance fee program. First, harbor maintenance activities, such as dredging by the Corps of Engineers, provide a commercial service to identifiable beneficiaries. Modern and well-maintained ports save shippers money through lower unit costs of shipping on larger vessels and by minimizing inland transport costs. Exporters currently make no payments directly associated with their use of port facilities. Second, imposing a harbor fee program would be unlikely to decrease port use because the fees would result in charges on users similar to the ones users recently paid under the rescinded tax.

Whether imposing a harbor fee system will pass constitutional muster is uncertain. Establishing such a system might be viewed by the Supreme Court as an unconstitutional export tax disguised by another name. A second legal concern with a fee program is whether it would violate international trade agreements, as several international trading partners allege of the harbor maintenance tax. Another drawback of the proposed fee system is that after several years, the cash it would generate would not keep pace with the revenue that the rescinded taxes would have generated. That is because tax collections based on the value of the goods shipped are projected to increase more quickly than the proposed fees, which would be tied to the costs of operating, constructing, and maintaining harbors.

300-13 Terminate Economic Support Fund Payments Under the South Pacific Fisheries Treaty

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	0	0
2002	0	0
2003	14	14
2004	14	14
2005	14	14
2001-2005	42	42
2001-2010	112	112
Relative to WIDI		
2001	0	0
2002	0	0
2003	15	15
2004	15	15
2005	15	15
2001-2005	45	45
2001-2010	125	125

SPENDING CATEGORY:

Discretionary

The South Pacific Fisheries Treaty is formally known as the Treaty on Fisheries Between the Governments of Certain Pacific Island States and the Government of the United States of America. Signed in April 1987, it lays out terms and conditions under which up to 55 U.S.-flag commercial fishing vessels may use purse seine methods to catch tuna in territorial waters of 16 Pacific Island states, including Kiribati, Micronesia, and Papua New Guinea. Japan, Korea, and Taiwan have similar treaties providing access to the waters for their tuna fleets.

Associated with the treaty is an agreement on annual economic assistance paid by the United States to the South Pacific Forum Fisheries Agency. The agreement provides for amending, extending, or terminating that arrangement by written agreement. In addition, either party may terminate the agreement by giving the other party one year's written advance notice. An amended agreement went into effect in 1993 providing for $14 million annually from June 1993 to June 2002. This option would terminate the U.S. government's payments to the South Pacific Forum Fisheries Agency at the end of the current agreement in 2003. Savings would total $112 million over the 2001-2010 period.

Currently, the treaty also provides for an annual industry payment that covers license fees for up to 55 vessels as well as technical assistance to the Pacific Island parties. In addition, the treaty calls for the U.S. tuna industry to cover the cost of the observer program. From June 1993 to June 1998, industry payments for licenses and technical assistance under the treaty were $4 million annually. For that same period, on average, 40 U.S.-flag vessels had access to tuna in the territorial waters of the South Pacific Island states each year. Thus, industry payments per vessel, excluding the cost of the observer program, averaged nearly $100,000 annually.

People in favor of terminating U.S. economic assistance under the treaty believe that taxpayers are supporting the access of private vessels to the territorial waters of the party states at an annual rate of over $340,000 per vessel. If those payments accurately reflect part of the value of that access to the fisheries, such a subsidy may encourage the overexploitation of fisheries.

People who oppose this option believe that the treaty is merely an expeditious vehicle, and the only vehicle, through which the United States provides financial assistance, in keeping with its foreign policy interests, to the nations in the South Pacific Forum Fisheries Agency. They argue that it is not a subsidy—the fishing industry's own payments under the treaty are comparable with those made by non-U.S. fleets. Those fleets obtain yearly licenses on a bilateral basis with any Pacific Island state of interest at a cost of 5 percent of the value of the previous year's catch.

300-14 Eliminate Federal Funding of Beach Replenishment Projects

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	90	45
2002	90	77
2003	90	90
2004	90	90
2005	90	90
2001-2005	450	392
2001-2010	900	842
Relative to WIDI		
2001	92	46
2002	94	79
2003	96	95
2004	98	96
2005	100	98
2001-2005	480	414
2001-2010	1,012	936

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

400-02

Each year, the U.S. Army Corps of Engineers partially funds and conducts several sand replenishment projects to counter beach erosion. That activity raises questions about the federal role in addressing what may be primarily local problems and the ultimate effectiveness of the replenishment efforts, without regard to who pays for them. These operations typically involve dredging sand from offshore locations and pumping it ashore to rebuild eroded areas. Typically, state and local governments share part of the operations' cost. Ceasing federal funding for beach replenishment activities would reduce discretionary outlays by $45 million in 2001 and $392 million for the 2001-2005 period.

Beach replenishment projects have two primary motivations: mitigating damage and enhancing recreation. Beaches act as a barrier to absorb wave energy and protect coastal property from severe weather. Replenishing eroded beaches helps them maintain that protective function. And because beaches are an important recreational resource in many areas, sand replenishment projects help to ensure that such areas continue to generate economic activity through tourism.

Opponents of federal spending for beach replenishment argue that its benefits accrue largely to the states and localities in which the projects occur. Therefore, such opponents reason, state and local governments should bear the projects' entire cost, not the federal government. Another argument against any funding, federal or otherwise, of replenishment projects is their ultimate futility. Beach erosion is an irreversible natural process, and replenishment projects serve only to temporarily delay the inevitable natural shifting of beaches. A better long-term solution would be to accept the fact that beaches will shift over time and to remove the various retention structures that inhibit the natural flow of sand along beaches and sometimes exacerbate erosion.

Supporters of replenishment projects argue that beach replenishment benefits the nation at large as well as specific states and localities. Advocates further contend that it would be unfair to stop federal funding, given the municipalities and property owners who have made investments with the expectation of continuing federal support. Supporters also argue that in some cases, federal projects—for example, those intended to keep coastal inlets open—contribute to beach erosion and that the federal government should bear part of the cost of replenishment in those cases.

300-15 Eliminate Energy-Efficiency Programs of the EPA

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	0	0
2002	64	54
2003	64	64
2004	64	64
2005	64	64
2001-2005	256	246
2001-2010	576	566
Relative to WIDI		
2001	0	0
2002	64	54
2003	66	65
2004	67	67
2005	69	69
2001-2005	266	255
2001-2010	637	625

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

270-04 and 270-08

The President's Climate Change Technology Initiative (CCTI) is a government-wide strategy to stabilize emissions of greenhouse gases. It includes several programs of the Environmental Protection Agency (EPA) that are intended to stimulate the adoption of energy-efficient technologies and the use of renewable energy by households and businesses. This option would halt new appropriations for two EPA activities that are a part of the CCTI but may contribute few environmental benefits: the Energy Star and Green Lights programs for labeling energy-efficient products and the Climate Wise program of public/private partnerships to encourage businesses to save energy.

Energy Star and Green Lights are product-labeling programs meant to encourage businesses to sell products that meet or exceed federal guidelines for energy efficiency and to raise consumers' awareness of energy-efficient products. The types of products that the EPA has designated to receive the labels include lighting fixtures, home appliances, office equipment, home construction material, and houses. The EPA also disseminates information on sellers of the labeled products and offers participants some technical assistance in implementing efficiency changes. The Climate Wise program assists businesses in identifying actions that may help them to save energy and reduce production costs, including free pollution-prevention and energy-efficiency assessments. For both programs, the main benefits to participants are in the public recognition and free advertising that they receive for their efforts.

Supporters of these EPA activities stress the relationship between energy use and emissions of greenhouse gases (primarily carbon dioxide) and other toxic or smog-producing elements—efforts to save energy may reduce such emissions. They also believe that the EPA is addressing market failures because consumers do not see the full public benefits of using energy-saving products. Insufficient consumer interest in energy efficiency may compound industry's normal disincentive to invest in uncertain new technologies.

Critics, however, question the actual energy savings and whether any savings that do occur would reduce greenhouse gas emissions. For example, putting a government label on products that already meet government standards may produce little gain. Also, encouraging consumers to purchase, for example, an electric appliance rather than a less-efficient gas appliance could actually increase carbon dioxide emissions, since the carbon content of the coal used to produce electricity is so high.

350

Agriculture

Budget function 350 covers programs administered by the Department of Agriculture, including such activities as agricultural research and stabilization of farm incomes through loans, subsidies, and other payments to farmers. CBO estimates that discretionary outlays for function 350 will total $4.5 billion in 2000. Mandatory outlays for the function will increase to an estimated $24.1 billion in 2000—from $7.9 billion in 1998—because of depressed commodity prices and provisions of the Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriation Act for Fiscal Year 2000.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	2.7	3.1	4.5	4.3	4.4	4.0	4.2	4.2	4.3	4.5	4.5
Outlays											
Discretionary	2.6	2.8	4.2	4.3	4.4	4.0	4.1	4.1	4.3	4.6	4.5
Mandatory	9.3	12.4	11.0	16.1	10.7	5.8	5.0	5.0	7.9	18.4	24.1
Total	12.0	15.2	15.2	20.4	15.0	9.8	9.2	9.0	12.2	23.0	28.5
Memorandum:											
Annual Percentage Change in Discretionary Outlays		6.6	49.2	1.9	3.1	-8.5	3.1	-1.5	6.3	5.5	-2.5

350-01 Reduce Federal Support for Agricultural Research and Extension Activities

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	186	122
2002	186	166
2003	186	182
2004	186	183
2005	186	183
2001-2005	930	836
2001-2010	1,860	1,751
Relative to WIDI		
2001	191	125
2002	196	174
2003	200	194
2004	205	200
2005	210	205
2001-2005	1,002	898
2001-2010	2,129	1,998

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

270-01, 270-02, 270-03, 270-04, 270-10, and 350-04

The Department of Agriculture (USDA) conducts and supports agricultural research and education. In particular, the Agricultural Research Service, the department's internal research arm, focuses on maintaining and increasing the productivity of the nation's land and water resources, improving the quality of agricultural products and finding new uses for them, and improving human health and nutrition. Those activities raise questions about the appropriateness and effectiveness of federal involvement. The Cooperative State Research, Education, and Extension Service (CSREES) participates in a nationwide system of agricultural research and educational program planning and coordination between state institutions and USDA. CSREES also takes part in the Cooperative Extension System, a national educational network that combines the expertise and resources of federal, state, and local partners. The Economic Research Service carries out economic and other social science research and analysis for public and private decisions about agriculture, food, natural resources, and rural America.

The 1999 appropriations for those three USDA units total $1.9 billion. Reducing the funding by 10 percent would save $836 million in outlays from 2001 to 2005 and about $1.8 billion from 2001 to 2010.

Federal funding for agricultural research may, in some cases, replace private funding. If federal funding was eliminated in those instances, the private sector would finance more of its own research. Moreover, federal funding for some extension activities under CSREES could be reduced without undercutting its basic services to farmers. For example, funding for the Nutrition and Family Education and Youth at Risk Programs totaled $68 million under the Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Act for Fiscal Year 2000.

Opponents of reducing funding for research and extension activities argue that the programs play important roles in developing an efficient farm sector. Reducing federal funding could compromise the sector's future development and its competitiveness in world markets. If the private sector assumed the burden of funding, agricultural research, which contributes to an abundant, diverse, and relatively inexpensive food supply for U.S. consumers, could decline. Moreover, some federal grants are used to improve the health of humans, animals, and plants by funding research that promotes better nutrition or more environmentally sound farming practices. If federal funding was cut back, the public might have to bear some of that cost in higher prices, forgone innovations, and environmental degradation.

350-02 Reduce Department of Agriculture Spending for Export Marketing and International Activities

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	31	21
2002	31	28
2003	31	31
2004	31	31
2005	31	31
2001-2005	155	142
2001-2010	310	297
Relative to WIDI		
2001	32	22
2002	33	30
2003	34	33
2004	34	34
2005	35	35
2001-2005	168	154
2001-2010	358	344

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

150-03, 350-06, and 350-09

The Department of Agriculture (USDA) promotes exports and international activities through the programs of the Foreign Agricultural Service (FAS). For example, in the Foreign Market Development Cooperator Program, FAS acts as a partner in joint ventures with "cooperators," such as agricultural trade associations and commodity groups, to develop markets for U.S. exports. FAS also collaborates on other ventures, one of which, the Cochran Fellowship Program, provides training to foreign nationals with the objective of improving commercial relationships that will benefit U.S. agriculture. Eliminating funding for those two programs would reduce outlays by $142 million over the 2001-2005 period and $297 million over the 2001-2010 period.

The Foreign Market Development Cooperator Program, also known as the Cooperator Program, typically promotes generic products and basic commodities, such as grains and oilseeds, but the program also covers some high-value products, such as meat and poultry. Some critics of the program argue that cooperators should bear the full cost of foreign promotions because the cooperators benefit from them directly. (How much return, in terms of market development, the Cooperator Program actually generates or the extent to which it replaces private expenditures with public funds is uncertain.) Some observers also cite the possibility of duplicative services because the USDA provides funding for marketing through its Market Access Program and other activities.

Eliminating the Cooperator Program, however, could place U.S. exporters at a disadvantage in international markets, depending in part on the amount of support other countries provide to their exporters. Regarding the issue of duplicative services, some advocates note that the Cooperator Program is distinct from other programs in part because it focuses on services to trade organizations and technical assistance. People concerned about U.S. exports of generic products and basic commodities consider the program useful for developing markets that could benefit the overall economy.

The Cochran Fellowship Program brings foreign midlevel managers to the United States for training in agriculture and agribusiness. Although the program is popular among recipients and their sponsors, its direct benefits to U.S. agriculture are unknown; thus, it may be marginally valuable to taxpayers. However, eliminating the Cochran Fellowship Program could hurt U.S. agriculture to the extent that the program builds commercial relationships, introduces foreign professionals to U.S. products, and creates new opportunities for U.S. exports.

350-03 Reinstate Assessments on Growers, Buyers, and Importers of Tobacco

	Savings (Millions of dollars) Budget Authority	Outlays
2001	8	8
2002	29	29
2003	30	30
2004	30	30
2005	30	30
2001-2005	127	127
2001-2010	277	277

SPENDING CATEGORY:

Mandatory

The federal government aids tobacco producers by supporting domestic tobacco prices above world-market levels. That support involves a combination of marketing quotas, price-supporting loans, and restrictions on imports. The support program benefits about 125,000 growers and 300,000 holders of marketing quotas and allotments. Some quota holders actually raise tobacco, and some rent their quota to others. For producers, tobacco is an important source of income, particularly in some states. The value of the 1998 tobacco crop was estimated at $2.8 billion. The crop is produced in 16 states, and about two-thirds of its acreage lies in North Carolina and Kentucky.

Tobacco is a controversial crop because of the health hazards of smoking, and federal support for producers has also been controversial. The price support program has been modified over time to reduce its costs to the taxpayer, even though it does nothing to encourage tobacco use. In fact, it raises the price of tobacco products to U.S. consumers but by a small amount. The Department of Agriculture has estimated that the program may increase the price of a pack of cigarettes by less than 2 cents.

The cost of the tobacco price support program varies from year to year. The program may have substantial outlays in a given year, but if it functions as intended, it should have no net cost to the government over time. The reason is that growers and purchasers of tobacco contribute to "no-net-cost accounts" that are used to reimburse the government for costs (excluding administrative costs) of the price support program. Starting with the 1991 crop, growers and purchasers each paid an additional assessment of 0.5 percent of the value of sales (for a total collection of 1 percent of sales). Those assessments, which were introduced to reduce the costs of federal farm programs and cut net federal outlays, expired with the 1998 tobacco crop. A related assessment on imported tobacco expired at the end of calendar year 1998. This option would reinstate those assessments beginning with the 2001 crop. Doing so would bring in receipts of $127 million over the 2001-2005 period.

The main benefit of reinstating the assessments is reducing net federal outlays. Proponents argue that the price support program gives tobacco producers substantial benefits and that the assessment recoups a portion of those benefits for the taxpayer. Opponents would argue that since the tobacco program costs the government little, assessments are unfair.

350-04 Eliminate Mandatory Spending for the Agricultural Research Activities of the Fund for Rural America and the Initiative for Future Agriculture and Food Systems

	Savings (Millions of dollars) Budget Authority	Outlays
2001	300	30
2002	150	105
2003	150	150
2004	0	150
2005	0	105
2001-2005	600	540
2001-2010	600	600

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

350-01

The Federal Agriculture Improvement and Reform Act of 1996 (FAIR) established the Fund for Rural America as a mandatory program to support rural communities nationwide. FAIR provided funds through fiscal year 2000. The Agricultural Research, Extension, and Education Reform Act of 1998 (Public Law 105-185) provided additional funds through 2003. Currently, $120 million is available for research activities of the Fund for Rural America for the 2001-2003 period.

In addition, the Agricultural Research, Extension, and Education Reform Act of 1998 created and provided mandatory funding for the Initiative for Future Agriculture and Food Systems as a competitive grants program supporting research, extension, and education activities in critical emerging areas. Administered by the Department of Agriculture's (USDA's) Cooperative State Research, Education, and Extension Service (CSREES), the initiative was mandated to receive $480 million through fiscal year 2003 to target food genome research, food safety, human nutrition, alternative uses for agricultural commodities, biotechnology, and precision agriculture. Eliminating those activities would reduce direct spending by $600 million from 2001 to 2010.

Mandatory funding is usually reserved for entitlement programs, for which funding needs may be too immediate or undisputed to warrant annual review by the Congress in the appropriation process. Supporters of this option argue that the programs should hardly be grouped with other entitlements and should be left where they have always been: as part of USDA's discretionary funding budget. Because providing the programs with mandatory funds may avoid the spending jurisdiction and annual review of the appropriations committees, supporters of the option argue that the programs do not necessarily provide funding for intended activities. In addition, they argue, existing discretionary programs can meet the goals of the agricultural research programs. Furthermore, they contend that federal funding for agricultural research may, in some cases, replace private funding. If federal funding was eliminated in those instances, the private sector would finance more of its own research.

Opponents of this option argue that reducing federal funding could compromise U.S. agriculture's future development and its competitiveness in world markets at a time when changes in commodity programs make producers' economic viability more dependent than before on world markets. They also argue that the programs are necessary to address future food productivity, environmental quality, and farm income.

350-05 Limit Future Enrollment of Land in the Department of Agriculture's Conservation Reserve Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	8	8
2002	132	132
2003	232	232
2004	321	321
2005	337	337
2001-2005	1,030	1,030
2001-2010	5,432	5,432

SPENDING CATEGORY:

Mandatory

The Conservation Reserve Program promotes soil conservation, improves water quality, and provides wildlife habitat by removing land from active agricultural production. Landowners contract with the program to keep land out of production, usually for a 10-year period, in exchange for annual rental payments. Such land is referred to as "enrolled" in the program. The federal government also pays part of what farmers spend to establish approved cover crops on the land. The Department of Agriculture's (USDA's) Commodity Credit Corporation funds the program and spends about $1.5 billion per year on it. The program now has roughly 30 million acres enrolled; the law limits enrollment to a total of 36.4 million acres. The Congressional Budget Office baseline assumes that future net enrollments of land will reach the limit by 2009. Stopping new enrollments beginning October 1, 2000, would reduce outlays by $1 billion over the 2001-2005 period and by $5 billion over the 2001-2010 period.

Some critics of the Conservation Reserve Program see it as corporate welfare—unnecessarily and inefficiently supporting farm income. Others see it as an expensive and poorly focused conservation program and believe that other uses of the money would yield greater environmental benefits. Still other critics worry about the loss of economic activity in areas where much crop land is retired. Demand for seed, fertilizer, and other farm supplies drops in such areas, hurting rural communities.

The Conservation Reserve Program enjoys widespread support, however. Landowners appreciate the payments, which often exceed profits from continued agricultural production and are more certain. Conservationists and environmentalists recognize the program's benefits and note USDA's plans to accept the most environmentally sensitive land in future enrollments. Those plans involve special provisions for enrolling land devoted to the most effective conserving practices such as the use of filter strips, grass waterways, and riparian buffers. Those and several other practices yield high returns per dollar spent in enhanced wildlife habitat, improved water quality, and reduced soil erosion. In fact, even most critics of the program recognize the need to take at least some environmentally sensitive land out of production for some time.

350-06 Eliminate Attaché Positions in the Foreign Agricultural Service

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	29	20
2002	39	33
2003	39	38
2004	39	39
2005	39	39
2001-2005	185	169
2001-2010	380	364
Relative to WIDI		
2001	30	20
2002	41	35
2003	42	41
2004	43	43
2005	44	44
2001-2005	200	183
2001-2010	440	420

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

350-02 and 370-02

U.S. agricultural attachés, located at 97 offices worldwide, provide U.S. agricultural producers and traders with information on foreign government policies, supply and demand conditions, commercial trade relationships, and market opportunities. That information is an integral part of the market forecasting and analysis system of the U.S. Department of Agriculture (USDA). The attachés, employed by the Foreign Agricultural Service of the USDA, also represent that department in disputes and negotiations with foreign governments on agricultural issues. The attaché positions were developed to promote U.S. commodities and to help U.S. farmers, processors, distributors, and exporters adjust their operations and practices to meet world conditions. This option would eliminate the attaché positions and reduce outlays by $169 million from 2001 to 2005 and $364 million from 2001 to 2010.

Proponents of eliminating the attaché positions argue that the federal government should not be collecting and distributing information that directly aids large private traders of agricultural commodities and products. Instead, they argue, private firms could collect such information. In addition, Department of State or Commerce personnel could assume the attachés' other functions. Although trade is vitally important to U.S. agriculture, according to that argument the industry no longer warrants the special treatment it receives.

Opponents of eliminating the agricultural attaché positions contend, however, that because attachés represent the U.S. government, they have more access to information than representatives of private firms would have. Opponents also maintain that if agricultural producers and traders do not receive quality agricultural information in a timely manner, the sector's responsiveness to changes in world demand for U.S. products could be compromised. Finally, USDA uses information collected by attachés in conducting its analyses. If the attachés no longer provided such information, USDA might have to purchase it; without it, USDA would have difficulty conducting policy analyses.

350-07 Reduce the Reimbursement Rate Paid to Private Insurance Companies in the Department of Agriculture's Crop Insurance Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	28	26
2002	30	30
2003	31	31
2004	32	32
2005	33	33
2001-2005	154	152
2001-2010	338	334

SPENDING CATEGORY:

Mandatory

The Federal Crop Insurance Program protects farmers from losses caused by drought, floods, pests, and other natural disasters. Insurance policies that farmers buy through the program are sold and serviced by private insurance firms, which receive an administrative cost reimbursement according to the total amount of insurance premiums they handle. Firms also share underwriting risk with the federal government and can gain or lose depending on the value of crop losses relative to claims made. Overall, the companies typically gain.

The General Accounting Office (GAO) has widely studied the crop insurance program and, in particular, the amount paid to the firms that service and sell the insurance policies. In a 1997 study, GAO concluded that the amount the program has paid the firms has historically exceeded the reasonable expenses of selling and servicing the crop insurance. Partly on the basis of that information, the 105th Congress cut the reimbursement rate for the benchmark crop insurance plan from 27 percent of premiums to 24.5 percent (with comparable reductions for other plans). This option would further reduce the benchmark rate to 22.5 percent, resulting in savings of $334 million over the 2001-2010 period.

Arguments for cutting the reimbursement rate hinge on the belief that the 105th Congress could have cut the reimbursement rate more deeply without substantially affecting the quantity or quality of services provided to farmers. In addition to relying on GAO's analysis, proponents of further cuts point to the dramatic expansion in business that followed enactment of the Federal Crop Insurance Reform Act of 1994. Total insurance in force for 1999 totals about $30 billion, which is over twice that of the early 1990s. Total premiums grew correspondingly, but because of economies of scale, the costs of selling and servicing the policies probably grew by less. Thus, proponents argue, the program could tolerate further cuts. Finally, even if cuts caused firms to curtail some services to farmers, proponents claim that the results would not be catastrophic or irreversible.

The industry argues, however, that the cuts enacted last year will impair its ability to sell and service insurance and will threaten farmers' access to insurance. If farmers lack insurance, the industry argues, the Congress would more likely resort to expensive, special-purpose disaster relief programs when disaster strikes, negating any apparent savings from cutting the reimbursement rate. That argument—perhaps made more forcefully—applies to any further program cuts. Moreover, falling crop prices reduce total premiums (and reimbursements) but hardly affect companies' costs. Cutting reimbursement rates would further reduce company profits, making it harder for them to maintain the services now provided to farmers.

350-08 Eliminate Public Law 480 Title I Sales and Limit the Secretary of Agriculture's Authority

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	150	79
2002	150	138
2003	150	146
2004	150	146
2005	150	146
2001-2005	750	655
2001-2010	1,500	1,385
Relative to WIDI		
2001	152	80
2002	155	142
2003	158	153
2004	160	155
2005	163	157
2001-2005	788	687
2001-2010	1,646	1,517

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

150-03

The U.S. Agricultural Trade Development and Assistance Act of 1954 (Public Law 480) was enacted to promote commercial exports of surplus agricultural commodities, foster foreign markets, and aid developing countries. The law included commodity sales for foreign currencies, concessional credit, and grants.

In the 45 years since the law was passed, the program may have become obsolete and inefficient. This option would eliminate sales under title I of the act beginning in 2001. It would also constrain authority provided by the Commodity Credit Corporation Charter Act of 1948 and other acts that allow the Secretary of Agriculture to use Commodity Credit Corporation or other funds to purchase and ship U.S. commodities abroad. Such constraints are necessary, some analysts believe, because without them, the Secretary of Agriculture could offset the effects of a cut in the program (a discretionary one) by using Commodity Credit Corporation or other funds (mandatory spending) to purchase and ship agricultural commodities. In fact, the Secretary used such authority in 1999 to provide more than $1 billion of food aid to Russia and other countries.

This option would reduce outlays by $655 million over the 2001-2005 period and by $1.4 billion over the 2001-2010 period. Title II of the act and section 416 of the Agricultural Act of 1949, which fund humanitarian and emergency feeding programs, would not be affected by this option.

The program's effectiveness in promoting agricultural exports is questionable for two reasons: exports under title I are a small portion of total U.S. agricultural exports, and the countries currently receiving those commodities are unlikely to become commercial customers. In fact, countries that receive commodities under title I are typically those in which the United States has a security or foreign policy interest rather than those likely to become commercial customers in the near term.

Providing assistance to developing countries is also a goal of the programs but may not always be an efficient use of U.S. resources. Many commodities that foreign countries buy with P.L. 480 assistance are resold to generate local currency. Those funds are used in turn to support local budgets and local development. But the inexpensive food may discourage local investment in agriculture, lower rural employment and income, and discourage the development of local stockpiles.

Supporters of title I argue that the programs are a flexible, fast means of providing assistance to friendly countries. They also note that the programs reduce the likelihood that agricultural surpluses will depress prices in the United States, and they stress the programs' humanitarian benefits: U.S. agricultural products are exported, and hungry people are fed.

350-09 Eliminate the Market Access Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	5	5
2002	73	73
2003	90	90
2004	90	90
2005	90	90
2001-2005	348	348
2001-2010	798	798

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

150-03 and 350-02

The Market Access Program (MAP), formerly known as the Market Promotion Program, was authorized under the 1990 Food, Agriculture, Conservation, and Trade Act to assist U.S. exporters of agricultural products. The program has been used to counter the effects of unfair trading practices abroad, but the Uruguay Round Agreements Act of 1994 eliminated the requirement that it be used for such purposes. Payments are made to partially offset the costs of market building and product promotion conducted by trade associations, commodity groups, and some profit-making firms. On the basis of current law, the Congressional Budget Office assumes that $90 million will be allocated annually for the program. Eliminating MAP would reduce outlays by $348 million over the next five years.

The program has been used to promote a wide range of mostly high-value products, including fruit, tree nuts, vegetables, meat, poultry, eggs, seafood, and wine. About 40 percent of MAP funding goes to promote brand-name products. The 1996 farm bill prohibits direct MAP assistance for brand promotions to foreign companies for foreign-produced products or to companies not recognized as small businesses under the Small Business Act, except for cooperatives and nonprofit trade associations.

Some critics of the program argue that participants should bear the full cost of foreign promotions because they benefit directly from them. (The extent to which the program has developed markets or replaced private expenditures with public funds is uncertain.) In addition, some critics note the possibility of duplication because the Department of Agriculture provides marketing funds through the Foreign Market Development Cooperator Program of the Foreign Agricultural Service and other activities. Many people also object to spending the taxpayers' money on advertising brand-name products.

Eliminating MAP, however, could place U.S. exporters at a disadvantage in international markets, depending in part on the amount of support provided by other countries. Responding to concerns about duplication, some MAP advocates note that the program differs from other programs partly because it focuses on foreign retailers and consumer promotions. People concerned about U.S. exports of high-value products consider the program useful for developing markets and benefiting the overall economy.

370

Commerce and Housing Credit

Budget function 370 covers programs administered by the Department of Commerce, the Federal Housing Administration, and the Small Business Administration, among others. They include programs to regulate and promote commerce and provide housing credit and deposit insurance. Also included in this category are outlays for loans and other aid to small businesses and support for the government's efforts to gather and disseminate economic and demographic data. CBO estimates that discretionary outlays for function 370 will total about $7.4 billion in 2000. That level—more than twice the 1999 figure—includes funding for the 2000 census.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	3.9	2.8	4.2	4.1	4.0	3.9	4.1	3.1	3.1	3.8	7.0
Outlays											
Discretionary	3.8	3.4	3.4	3.7	3.4	3.7	3.5	3.4	3.2	3.5	7.4
Mandatory	63.8	72.9	7.5	-25.6	-7.6	-21.5	-14.0	-18.0	-2.2	-0.9	-2.5
Total	67.6	76.3	10.9	-21.9	-4.2	-17.8	-10.5	-14.6	1.0	2.6	4.9
Memorandum:											
Annual Percentage Change in Discretionary Outlays		-12.6	1.0	9.7	-9.1	10.3	-6.2	-4.0	-5.3	10.6	111.4

370-01 End the Credit Subsidy for Major Small Business Administration Business Loan Guarantee Programs

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	125	80
2002	125	118
2003	125	120
2004	125	120
2005	125	120
2001-2005	625	558
2001-2010	1,250	1,158
Relative to WIDI		
2001	127	81
2002	129	121
2003	131	125
2004	134	128
2005	136	130
2001-2005	657	585
2001-2010	1,372	1,267

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

370-05

The Small Business Administration (SBA) operates several loan guarantee programs to increase small businesses' access to capital and credit. Under the Federal Credit Reform Act of 1990, the credit subsidy for those programs is the estimated net present-value cost of projected defaults (excluding administrative costs) to the SBA of guaranteeing loans over their lives. SBA's largest business credit programs are the general business loan guarantee, or 7(a) program; the certified development company, or 504 program; and the small business investment company (SBIC) equity capital programs. One of the programs, the certified development company loan program, now operates with a zero subsidy rate. Equalizing the subsidy rate of all major SBA business loan guarantee programs at zero would reduce outlays by $1.2 billion for the 2001-2010 period measured against the 2000 funding level.

Under the 7(a) loan guarantee program, the federal government guarantees 80 percent of the principal for business loans up to $100,000 and 75 percent of the principal for larger ones. Small business investment companies in the SBIC program are private investment firms licensed by the SBA. They make equity investments and long-term loans to small firms, using their own capital supplemented with SBA-guaranteed debentures.

In 1996, the Congress amended both the Small Business Act and the Small Business Investment Act to reduce subsidy rates and improve the performance of the SBA's business loan programs. One of the most significant changes the Congress made was to increase the fees paid by loan recipients for most business loans. Those increases help to reduce program costs because the revenues from the fees cover some of the expenses if a borrower defaults. The Congress also cut the percentage of each loan amount that the government guarantees under the SBA's largest loan program—the 7(a) program—from about 90 percent to about 80 percent. Reducing the guarantee rate should induce banks to more carefully evaluate loan applications because the banks will share more responsibility for any losses from defaults. If banks use more care in approving SBA loans, the default rate should decline, and the program's cost to the government should decrease. Adjusting fees (and changing loan guarantee levels) to cover potential default losses could make the major SBA business loan programs financially sound. As the subsidy rate declined to zero, the Congress would no longer have to appropriate funds to cover the government's expected losses.

Critics of this option believe SBA assistance aids small businesses by filling a gap in financing when banks and other traditional sources do not provide loans for the purposes, in the amounts, and with the terms required by small business borrowers. Some critics argue against increasing program fees or reducing guarantee rates because such changes would reduce access to credit for small businesses. Others argue that subsidies are not necessary because the loan programs provide the mechanism to pool risk so that the private sector will make financing available. Some supporters of this option argue, however, that SBA assistance serves only a tiny fraction of the nation's small businesses and that most of the program's borrowers could obtain financing without the SBA's help.

370-02 Reduce Costs of the ITA by Eliminating Trade Promotion Activities or Charging the Beneficiaries

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	61	43
2002	244	183
2003	244	225
2004	244	244
2005	244	244
2001-2005	1,037	939
2001-2010	2,257	2,159
Relative to WIDI		
2001	63	44
2002	260	195
2003	267	245
2004	275	272
2005	283	279
2001-2005	1,148	1,035
2001-2010	2,684	2,554

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

300-05, 400-05, and 400-06

RELATED CBO PUBLICATIONS:

Antidumping Action in the United States and Around the World: An Analysis of International Data (Paper), June 1998.

How the GATT Affects U.S. Antidumping and Countervailing-Duty Policy (Study), September 1994.

The International Trade Administration (ITA) of the Department of Commerce has four major program activities: the Import Administration, which investigates antidumping and countervailing-duty cases; the trade development program, which assesses the competitiveness of U.S. industries and runs export promotion programs; the market access and compliance (MAC) unit, which works to unlock foreign markets for U.S. goods and services; and the U.S. and foreign commercial services, which counsel U.S. businesses on exporting. The MAC unit, and perhaps the countervailing-duty program against foreign subsidies, may be necessary to maintain public support for free-trade policies, and in some cases, they can be defended on economic grounds. The ITA's export promotion, marketing, and counseling activities could be eliminated, however, or the beneficiaries could be charged fees to cover more of the programs' costs. The ITA already charges some fees for some services, but those fees do not cover the cost of all such activities.

Some people argue that such activities are better left to the firms and industries involved rather than to the ITA. Others argue that those activities might have some economies of scale, especially for small firms. If so, having one entity (the federal government) counsel exporters on foreign legal and other requirements, disseminate knowledge of foreign markets, and promote U.S. products abroad might make sense. In that case, net federal spending could be reduced by charging the beneficiaries of those programs their full cost.

Fully funding the ITA's trade promotion activities through charges that are voluntary for all beneficiaries may not be possible, however. For example, in many cases, promoting the products of selected firms in a given industry that want and pay for such promotion may be impossible without also encouraging demand for the products of all other firms in that industry. In those circumstances, all the firms have an incentive not to purchase the services because they know that they are likely to receive the benefits whether they pay for them or not. Consequently, if the federal government wanted to charge beneficiaries for the ITA's services, it might have to require that all firms in an industry (or the industry's national trade group) decide together whether to purchase the ITA's services. If the firms decided to purchase them, all firms in the industry would be required to pay according to some equitable formula.

When beneficiaries do not pay the full cost of services, the ITA's activities effectively subsidize the industries involved. Those implicit subsidies are an inefficient means of helping the industries because they are partially passed on to foreigners in the form of lower prices for U.S. exports. Because the current-account balance is determined by total saving and investment in the U.S. economy, over which the ITA has no influence, the agency's activities do not improve the current-account balance. As a result of the changes they cause in exchange rates and other variables, some combination of reduced exports in other industries and increased imports completely offsets all increases in exports resulting from ITA activities. Thus, the ITA's export promotion activities hurt other U.S. firms.

370-03 Eliminate the Advanced Technology Program

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	114	11
2002	143	43
2003	143	96
2004	143	136
2005	143	143
2001-2005	686	429
2001-2010	1,401	1,144
Relative to WIDI		
2001	117	12
2002	149	44
2003	151	99
2004	154	142
2005	157	152
2001-2005	728	449
2001-2010	1,560	1,252

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

370-04

The Omnibus Trade and Competitiveness Act of 1988 established the Advanced Technology Program (ATP) within the Commerce Department's National Institute of Standards and Technology. This option would eliminate the ATP, whose objective is to further the competitiveness of U.S. industry by helping convert discoveries in basic research more quickly into technological advances with commercial potential. The program awards research and development (R&D) grants on the basis of merit to individual companies, independent research institutes, and joint ventures. The grants support research in generic technologies that have applications for a broad range of products as well as precompetitive research (preceding product development). This option would eliminate the ATP, saving $1.1 billion through 2010.

The ATP's grants are limited to $2 million over a three-year period when awarded to a single firm, but they have no dollar limit when awarded to a joint venture over a period of up to five years. Joint ventures must pay at least half of the R&D costs of each project, however, which helps ensure a project's commercial viability.

The ATP has awarded 468 grants from its inception through 1999, including awards to 157 joint ventures. Roughly two-thirds of the firms participating in awards are small or medium-sized firms or joint ventures led by small or medium-sized firms; large firms account for only 20 percent of grant recipients. Universities and other nonprofit organizations participated in 256 projects as joint-venture partners. Total funding committed to the research projects was $3.0 billion, of which the ATP paid roughly half.

Starting in 1998, the ATP explicitly required applicants to disclose their prior efforts to secure private financing. ATP officials also made consideration of spillover benefits part of the selection criteria. The ATP was responding to earlier research done by the General Accounting Office (GAO), which found that almost two-thirds of applicants had not even sought private capital before applying to the ATP and that half of the proposals the ATP rejected were subsequently funded privately. GAO found that the changes in the selection process, although positive, are insufficient, rely on the self-interested applicants for crucial information, or are difficult to operationalize.

Opponents of the program argue that private investors, not the federal government, are better able to decide which research efforts should be funded. Furthermore, citing the GAO survey, critics argue that even when the federal government chooses "a winner," it is just as likely as not to be displacing private capital. The U.S. venture capital markets are the best developed in the world and do an effective job of funding new ideas.

Program supporters argue that surveys of the ATP's award recipients indicate that the awards have accelerated the development and commercialization of advanced technology by two years or more in the majority of planned commercial applications. In addition, those surveys reveal that recipients are more willing to tackle high-risk technology development projects as a result of their grants, presumably increasing both the amount and the breadth of the R&D funded.

370-04 Eliminate the Manufacturing Extension Partnership and the National Quality Program

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	87	11
2002	109	36
2003	109	75
2004	109	104
2005	109	109
2001-2005	523	335
2001-2010	1,068	880
Relative to WIDI		
2001	89	11
2002	113	37
2003	116	77
2004	118	109
2005	120	116
2001-2005	556	350
2001-2010	1,194	968

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

370-03

The Manufacturing Extension Partnership (MEP) and the National Quality Program reside in the National Institute of Standards and Technology. MEP consists primarily of a network of manufacturing extension centers that assist small and midsize firms with expertise in the latest management practices, manufacturing techniques, and other knowledge. The nonprofit centers are not owned by the federal government but are partly funded by it. The National Quality Program consists mainly of the Malcolm Baldrige National Quality Award, which is given to firms for achievements in quality. This option would eliminate the MEP and the National Quality Program, saving $880 million through 2010.

Proponents of MEP point to the economic importance of small and midsize firms, which produce more than half of U.S. output and employ two-thirds of U.S. manufacturing workers. Small firms, they argue, often face limited budgets, lack of expertise, and other barriers to obtaining the information that MEP provides. Those circumstances and the substantial reliance of larger firms on small and midsize companies for supplies and intermediate goods lead proponents to contend that MEP is needed for U.S. productivity and international competitiveness.

Opponents may question the need for government to provide such technical assistance. Small firms thrived long before MEP began in 1989, in part because other sources of expertise were available. Many professors of business, science, and engineering are also consultants to private industry, and other ties between universities and private firms facilitate the transfer of knowledge. In fact, some of the centers MEP subsidizes predate MEP.

Furthermore, MEP cannot improve the competitiveness of the economy as a whole. The competitiveness of particular firms helped by MEP may improve, resulting in more exports or fewer competing imports. However, those changes in trade cause the dollar to rise in foreign exchange markets, decreasing the competitiveness of other U.S. firms. Overall, the balance of trade is not affected.

Finally, one may question MEP's positive effect on the economy's productivity. Federal spending for MEP is a subsidy for the firms MEP helps. In most cases, subsidies promote inefficiency by allowing inefficient firms to remain in business, tying up capital, labor, and other resources that would otherwise be used more productively elsewhere. In the case of businesses that increase their exports, part of the subsidy is likely to be passed on to foreign customers in the form of lower prices.

Like MEP advocates, defenders of the National Quality Program argue that it promotes U.S. competitiveness. The same counterargument used for MEP also applies to the National Quality Program. Opponents may argue that businesses need no government incentive to maintain quality—the threat of lost sales is sufficient. Furthermore, winners of the Baldrige Award often mention it in their advertising, which means they value it. If so, they should be willing to pay contest entry fees large enough to eliminate the need for federal funding.

370-05 Eliminate the Minority Business Development Agency

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	22	6
2002	27	25
2003	27	27
2004	27	27
2005	27	27
2001-2005	130	112
2001-2010	265	247
Relative to WIDI		
2001	23	7
2002	28	26
2003	29	28
2004	30	29
2005	30	30
2001-2005	140	120
2001-2010	302	280

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

370-01

The Minority Business Development Agency (MBDA) of the Department of Commerce plays the lead coordinating role in all federal programs for minority business development. Through public/private partnerships, the MBDA provides a variety of direct and indirect business services. It provides management and technical assistance, expands domestic and international marketing opportunities, and collects and disseminates business information. The agency also provides support for advocacy, research, and technology to reduce information barriers. This option would eliminate the MBDA, saving $247 million over the 2001-2010 period.

The arguments for and against the MBDA mirror in part those of the larger debate over affirmative action. Proponents contend that minority groups, especially African Americans, have historically been, and continue to be, hindered by pervasive discrimination. They argue that such discrimination leads to financial and educational disadvantage and lack of experience, which means that members of minority groups are less competitive relative to (non-Hispanic) whites in the business world. Discrimination also hinders minority businesses in their task of developing business relationships with suppliers and customers. Minorities, according to the program's advocates, need a helping hand to compensate for those unfair handicaps.

Opponents maintain that discrimination has substantially declined and that which remains is best fought by enforcing civil rights laws in the courts. Although, on average, African Americans and certain other minority groups are economically and educationally disadvantaged in comparison with whites, in many individual instances the reverse is true: individual African Americans or members of other minorities may be quite wealthy and educated and are competing with individual whites who are not. In such cases, opponents point out, a desire to help the disadvantaged would argue for helping the white person—not the minority group member. It is unfair, according to that argument, to help current-generation minority individuals at the expense of current-generation whites simply because previous generations of whites benefited from discrimination against previous generations of minorities. Opponents contend that such help should be limited to remedies for specific acts of illegal discrimination that have been proved in court or to general help for anyone who is disadvantaged, regardless of race. If the MBDA was eliminated, the Small Business Administration would continue to provide assistance to small businesses in general.

370-06 Eliminate the 85 Percent Market Adoption Test for Digital Television

	Added Receipts (Millions of dollars)
2001	0
2002	300
2003	300
2004	0
2005	0
2001-2005	600
2001-2010	600

SPENDING CATEGORY:

Mandatory

The Balanced Budget Act of 1997 (BBA) requires the Federal Communications Commission (FCC) to auction licenses to use certain parts of the radio spectrum made available by the transition from analog television broadcasting to digital television broadcasting that is now in progress. Those parts of the spectrum will not be available for use by auction winners until 2007 at the earliest; they will not be available until even later in markets in which less than 85 percent of the households are able to receive a digital television signal. The BBA further stipulates that the receipts from the auction must be deposited in the Treasury no later than September 30, 2002. This option would eliminate the 85 percent market adoption test, which the Congressional Budget Office estimates will increase auction receipts by $600 million.

As mandated by law, the nation's television broadcasters are currently shifting their operations from a technology based on analog signals to a newer, higher capacity-signal system based on digital technology. Current law anticipates that the transition from analog to digital broadcasting will be completed by the end of 2006, but it also provides for extending the transition if less than 85 percent of the households in a television market are able to receive the new digital signal at that time. Once the 85 percent adoption test is met and the transition is deemed complete, broadcasters in that market will stop broadcasting the old analog signals. The move to a digital system may require households to invest in new equipment before they can receive the new signals.

Current law also stipulates that the rights to use certain parts of the radio spectrum freed by the adoption of the digital television standard must be auctioned before the transition is complete. Thus, even with a timely transition, bidders will be making their offers with the understanding that the licenses they bid on will not permit full use of the associated spectrum until the transition's end. Since the BBA was enacted, however, it has become increasingly clear that the 85 percent goal probably will not be met in many markets by 2006 and that the transition will be extended in those areas. As the time between paying for and making profitable use of the spectrum freed by the transition appears to be lengthening, estimates of the receipts that will be raised by selling the rights to use it have been revised downward. Eliminating the 85 percent exemption and guaranteeing that the transition will not continue beyond the end of 2006 would decrease the time between the auction and the spectrum's availability and, consequently, increase receipts.

The argument in favor of this option rests on the economic value created by the earlier availability for other purposes of a portion of the frequencies currently allocated to television broadcasting. That argument is based on the conjecture that the new uses of the spectrum in question will be more valuable than the losses in television viewing created by a more rapid transition. Viewers who do not adopt digital television by 2006, the option's proponents might say, do not highly value television, and thus the social loss of disenfranchising them is correspondingly small. In the current case, higher auction receipts are a by-product of the radio spectrum's being used more efficiently.

The main argument against this option emphasizes the economic and social costs of ending the transition before the 85 percent market penetration level is reached. Those households that are last to adopt digital television and most likely to be disenfranchised by an earlier end to the transition may be the households that are least able to afford the equipment required for the upgrade to digital televison. In addition, depriving more than 15 percent of the population of free, over-the-air broadcast television may be an undesirable social consequence.

370-07 Charge a User Fee on Commodity Futures and Options Contract Transactions

	Savings (Millions of dollars) Budget Authority	Outlays
2001	62	62
2002	62	62
2003	62	62
2004	62	62
2005	62	62
2001-2005	310	310
2001-2010	620	620

CATEGORY:

This fee could be classified as a discretionary offsetting collection, a mandatory offsetting receipt, or a revenue depending on the specific language of the legislation establishing the fee.

The Commodity Futures Trading Commission (CFTC) administers the amended Commodity Exchange Act of 1936. The purpose of the commission is to allow markets to operate more efficiently by ensuring the integrity of futures markets and protecting participants from abusive and fraudulent trade practices. A fee on transactions overseen by the CFTC could cover the agency's operating costs. Such a fee would be similar to one now imposed on securities exchanges to cover the operating costs of the Securities and Exchange Commission (SEC).

A per-contract transaction fee could be imposed and remitted quarterly and adjusted periodically so that the money collected equals the CFTC's cost of operation. Meeting the CFTC's operating expenses of $620 million over the 2001-2010 period would require a nominal fee of around 10 cents per contract, assuming that the number of contracts traded annually over the period remains near the number traded in 1999. The CFTC would collect the fee. The Congressional Budget Office envisions that authorizing legislation would establish the fee, but only appropriation language would trigger the collection of the fee. The fee would then be classified as an offsetting collection.

The main arguments for the fee are based on the principle that users of government services should pay for those services. Participants in transactions that the CFTC regulates, rather than general taxpayers, are seen as the main beneficiaries of the agency's operations and therefore should pay a fee, according to proponents of the fee. Furthermore, the precedent for charging user fees has already been established by the SEC and other federal financial regulators, such as the Office of Thrift Supervision and the Office of the Comptroller of the Currency. Considerations of equity and fairness suggest that not charging a comparable fee to support CFTC operations could give futures traders an unfair advantage over securities traders.

People who argue against the fee maintain that such charges tend to encourage evasion by those who have to pay them. Users might try to avoid fees by limiting or shifting transactions to activities that are exempt from charges, which could conceivably cause some market participants to desert U.S. exchanges for foreign exchanges. Major competing foreign exchanges, however, already charge transaction fees. Even with a nominal fee, U.S. futures exchanges may still have a cost advantage over their major foreign competitors.

CBO expects a fee of around 10 cents to cause a negligible decrease in transactions because that fee is small compared with fees already imposed by the exchanges and the industry's self-regulatory organization, the National Futures Association.

370-08 Eliminate FHA Mortgage Insurance Rebates

	Savings (Millions of dollars) Budget Authority	Outlays
2001	240	240
2002	240	240
2003	240	240
2004	240	240
2005	240	240
2001-2005	1,200	1,200
2001-2010	2,400	2,400

SPENDING CATEGORY:

Mandatory

The Federal Housing Administration (FHA) insures home mortgages made by private lenders. It assumes the default risk on loans to eligible home buyers, who usually make down payments of 5 percent or less and often have debt payment burdens that are high relative to their income. The agency charges both up-front and annual insurance premiums to cover its default losses. The up-front premium equals 2.25 percentage points of the mortgage amount; the annual premium equals 0.5 percentage points of the outstanding loan balance. The FHA partially refunds the up-front premium if the borrower pays off the mortgage in full during the first seven years. If the borrower takes out a new loan that the FHA insures, the refund is credited toward the up-front premium on the new loan. If the rebate and the equivalent credit were eliminated for newly insured loans, the government would save $240 million in 2001 and $1.2 billion over five years. Over 10 years, the savings would total $2.4 billion.

Eliminating the rebate would raise the cost of FHA insurance, which could lead some borrowers to take their business to the private mortgage insurance industry rather than to the FHA. Borrowers who pose less default risk than the average ones served by the FHA would be most likely to do that because they are most likely to exercise their prepayment option. Given the FHA's forecast of prepayment rates on newly insured loans, eliminating the rebate would be equivalent to increasing the up-front premium by about $2.50 for every $1,000 borrowed (25 basis points). Many borrowers probably do not place a high value on the rebate when deciding whether to use FHA or private insurance.

Eliminating the rebate of the FHA's up-front premium would make it easier for prospective FHA borrowers to evaluate the cost of the agency's insurance. It would also have the advantage of better directing FHA insurance to borrowers in need of government assistance. But the resulting increase in the relative cost of FHA insurance could hamper the agency's ability to attract low-risk borrowers, whose presence helps to maintain an actuarially sound insurance program. Because eliminating the rebate would probably not cause many low-risk borrowers to take their business elsewhere, however, it would probably have little effect on the soundness of the program. (The most effective way to ensure the program's soundness would be to introduce greater variation in FHA premiums based on a borrower's default risk.) In addition, raising the cost of FHA insurance by eliminating the rebate could cause some higher-risk borrowers to delay their home purchases or buy smaller homes. Because the FHA has a strong market presence among younger borrowers and low- and moderate-income and minority borrowers and neighborhoods, those home buyers and areas would most likely be affected. Whether higher-risk FHA borrowers account for the value of the rebate in deciding on the size and timing of their home purchases is unclear, however.

370-09 Increase the Ginnie Mae Guarantee Fee

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	40	40
2002	40	40
2003	40	40
2004	40	40
2005	0	0
2001-2005	160	160
2001-2010	160	160
Relative to WIDI		
2001	40	40
2002	40	40
2003	40	40
2004	40	40
2005	0	0
2001-2005	160	160
2001-2010	160	160

NOTE: Although Ginnie Mae is characterized as a discretionary program, this option would save the same amounts under a WODI and WIDI baseline.

SPENDING CATEGORY:

Discretionary

The Government National Mortgage Association, or Ginnie Mae, is a government corporation that facilitates the financing of federally insured and guaranteed home mortgages. Ginnie Mae guarantees mortgage-backed securities (MBSs) collateralized by home mortgages that are insured by the Federal Housing Administration (FHA) or guaranteed by the Department of Veterans Affairs or the Department of Agriculture's Rural Housing Service. Ginnie Mae now charges issuers an annual fee of 6 cents for every $100 (6 basis points) of guaranteed MBSs backed by single-family loans. Under current law, a fee increase to 9 basis points is scheduled to take effect in 2005. Moving the fee hike up to 2001 would save $40 million in 2001 and $160 million over five years.

The cost of the fee increase would be shared by two groups: the firms that issue and service the mortgages backing MBSs guaranteed by Ginnie Mae, and borrowers who take out such loans. Ginnie Mae issuers would lose income from a reduction in their servicing fee from the current maximum of 44 basis points to 41 basis points (federal law limits the sum of the Ginnie Mae guarantee and servicing fees to 50 basis points). A Ginnie Mae servicing fee of 41 basis points would probably still surpass competitive levels, which has the benefit of inducing issuers to diligently service loans. Some issuers with low profit margins would leave the market as a result, but other firms in this highly competitive industry would increase their business. Issuers leaving the business would prefer to sell their portfolios rather than default, so Ginnie Mae's default costs would probably be unaffected.

Alternatively, some issuers of Ginnie Mae MBSs might try to maintain their profit margins by raising the interest rates on the new federally insured or guaranteed mortgages they made. Fully passing on to borrowers the cost of an increase of 3 basis points in the guarantee fee would raise the monthly payments on a $100,000 loan by $2.50. An increase of that size would probably have little effect on the demand for federally insured and guaranteed mortgages or the volume of Ginnie Mae MBSs issued. Borrowers take out such loans mainly because the government accepts lower down payments and has less stringent underwriting guidelines than do private mortgage insurers.

Proponents of raising the Ginnie Mae guarantee fee by 3 basis points argue that the hike would result, at most, in a modest increase in the cost of using FHA mortgage insurance that would lead few, if any, borrowers to switch to private mortgage insurance. In addition, proponents argue that a modest reduction in the profitability of issuers of Ginnie Mae MBSs would not adversely affect the policy objective of ensuring a steady supply of credit to housing. Opponents of moving up the fee hike argue that any increase in the cost of using FHA mortgage insurance or the Department of Veterans Affairs' loan guarantees is unwarranted. They are also concerned about the precedent of raising the fee, which could open the door to later increases that could jeopardize the viability of many Ginnie Mae issuers or hasten the consolidation of the mortgage banking industry.

370-10 Require All GSEs to Register with the SEC

	Added Receipts (Millions of dollars)
2001	313
2002	304
2003	294
2004	274
2005	274
2001-2005	1,459
2001-2010	2,109

NOTE: Most of the additional receipts would be revenues; a portion of the fees would be offsetting collections credited against discretionary spending.

RELATED OPTION:

920-04

RELATED CBO PUBLICATIONS:

Assessing the Public Costs and Benefits of Fannie Mae and Freddie Mac (Report), May 1996.

Controlling the Risks of Government-Sponsored Enterprises (Report), April 1991.

Government-sponsored enterprises (GSEs) are private financial institutions chartered by the federal government to support the flow of funds to agriculture, housing, and higher education. GSEs achieve their public purposes by borrowing on the strength of an implicit federal guarantee of their debt obligations. The implicit guarantee lowers GSEs' cost of borrowing, conveying subsidies that give them a competitive advantage in financial markets. The federal government also explicitly subsidizes five GSEs—Fannie Mae, Freddie Mac, the Federal Home Loan Bank System, the Farm Credit System, and Sallie Mae—by exempting them from the registration requirements of the Securities Act of 1933. That statute requires all corporations issuing stock or debt securities with maturities of more than nine months to register such offerings with the Securities and Exchange Commission (SEC), disclose uniform information about the securities, and pay registration fees. A sixth enterprise, Farmer Mac, is not exempt from SEC registration. In 1992, the Department of the Treasury, the Federal Reserve, and the SEC advocated requiring the five GSEs that are now exempt to register their securities with the SEC, which would save $313 million in 2001, $1.5 billion over five years, and $2.1 billion through 2010.

Requiring issuers to register their securities with the SEC protects investors by ensuring that all offerings are accompanied by disclosures of uniform information. GSEs were originally exempted from the requirement in part to relieve them of the costs of registering until they became accepted names in the marketplace. That rationale no longer applies: the five exempt GSEs are well known in financial markets. Repealing the exemption would not impose significant additional regulatory burdens on those GSEs because they now disclose most of the required information voluntarily. Moreover, it would reduce the competitive advantage that the enterprises have over other firms that finance loans by issuing debt or mortgage-backed securities (MBSs). (Although bank securities are exempt from the registration requirements of the 1933 act, the securities of bank holding companies and all MBSs issued by non-GSEs are not.) A more level playing field would probably lead to a more efficient allocation of credit.

To register with the SEC, each of the five GSEs would pay about 25 cents for every $1,000 (about 2.5 basis points) in securities it issued in 2001. SEC registration fees are scheduled to decline gradually under current law and will be less than 1 basis point in 2007 and later years. Competition from wholly private firms and between the enterprises would limit the GSEs' ability to recoup the cost of paying registration fees by raising the interest rates on the loans they finance. Fully absorbing the costs of registration would have little effect on either the enterprises' profits or the interest rates paid by the borrowers they serve. If Fannie Mae absorbed the full cost of registering its securities, for example, that GSE's after-tax return on equity would probably decline by less than 1 percentage point. But if Fannie Mae and Freddie Mac lowered the prices they pay for the home mortgages they buy to cover the full cost of registering securities issued to finance such loans, the origination fees paid by homeowners with loans with an initial balance of $150,000 would rise by less than $38.

370-11 Eliminate New Funding for the Rural Rental Housing Assistance Program

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	45	3
2002	45	23
2003	45	34
2004	45	43
2005	45	44
2001-2005	225	147
2001-2010	450	368
Relative to WIDI		
2001	46	3
2002	46	23
2003	47	35
2004	48	45
2005	49	46
2001-2005	236	152
2001-2010	493	398

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

600-02, 600-05, and REV-30

The Section 515 housing program, administered by the Rural Housing Service (RHS), provides low-interest mortgage loans to developers of multifamily rental projects in rural areas. Those mortgages typically have credits that reduce the effective interest rate to 1 percent and, in turn, lower rental costs for Section 515 tenants.

Under current rules, assisted tenants pay rent equal to the greater of 30 percent of their adjusted income or the basic rent. (The basic rent for each unit consists of a proportionate share of the amortization costs of the 1 percent mortgage and the project's operating expenses.) The owner of the housing project keeps the basic rent, and the RHS collects any payments above it. Many of the poorest tenants receive additional federal subsidies through the Rural Rental Assistance Payments program that reduce their rent payments to 30 percent of their income.

Eliminating all new commitments for assistance under the Section 515 program would reduce federal outlays by about $368 million over the 2001-2010 period.

Support for this option is based on the view that expanding rural rental assistance is inappropriate when other federal programs are being cut. In addition, turnover among current project residents would ensure that the program would help some new income-eligible families each year.

Critics of this option point out that it would reduce the proportion of rural families the program can help as the number of eligible families continues to grow. Moreover, eliminating new funding for the program would slow the growth in the supply of standard-quality, low-income rental units in rural areas.

400

Transportation

Budget function 400 covers most programs of the Department of Transportation as well as aeronautical research by the National Aeronautics and Space Administration. It supports programs that aid and regulate ground, air, and water transportation, including grants to states for highways and airports and federal subsidies for Amtrak. CBO estimates that total outlays for function 400 will be $47 billion in 2000. Almost all of that amount is classified as discretionary spending. (Funding for most transportation programs is provided by mandatory contract authority.) Over the past 10 years, spending under function 400 has increased significantly.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	13.5	13.7	15.0	14.0	15.7	12.5	13.6	14.5	16.0	13.7	14.5
Outlays											
Discretionary	27.9	29.3	31.5	33.3	36.0	37.1	37.1	38.4	38.3	40.6	44.7
Mandatory	1.6	1.8	1.9	1.7	2.1	2.3	2.5	2.3	2.1	1.9	2.3
Total	29.5	31.1	33.3	35.0	38.1	39.4	39.6	40.8	40.3	42.5	47.0
Memorandum:											
Annual Percentage Change in Discretionary Outlays		5.0	7.5	5.6	8.3	2.9	0	3.7	-0.4	6.0	10.2

400-01 Eliminate Federal Subsidies for Amtrak

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	0	0
2002	0	0
2003	571	228
2004	571	571
2005	571	571
2001-2005	1,713	1,370
2001-2010	4,568	4,225
Relative to WIDI		
2001	0	0
2002	0	0
2003	600	240
2004	610	604
2005	621	614
2001-2005	1,831	1,458
2001-2010	5,096	4,691

SPENDING CATEGORY:

Discretionary

When the Congress established the National Railroad Passenger Corporation, commonly known as Amtrak, in 1970, it anticipated providing subsidies for only a limited time, until Amtrak could become self-supporting. By 1999, however, Amtrak had consumed more than $20 billion in federal subsidies. In addition to subsidies made through annual appropriations, the Congress gave Amtrak $2.2 billion (in the form of credits for tax refunds) under the Taxpayer Relief Act of 1997. That money was to be used for investments that would help turn Amtrak around. Further, the Amtrak Reform and Accountability Act of 1997 (ARAA) requires that Amtrak be self-supporting on an operational basis by the end of 2002.

This option would eliminate all federal subsidies for Amtrak by the end of 2002. Amtrak would have to finance its capital investments without federal assistance. To help make up for that loss of federal funding, the Congress could authorize states to use federal-aid highway funds for Amtrak. This option would save $4.2 billion over the 2001-2010 period.

Proponents of eliminating federal subsidies contend that Amtrak should be self-supporting, as initially envisioned. Without federal subsidies, Amtrak would have to focus on service that has the greatest potential for financial success, such as the Metroliner's high-speed service along the congested corridor between Washington and New York City, where passengers are willing and able to pay the full cost of the service. Amtrak would be forced to continue to improve efficiency in its operations and its investments. Those who favor eliminating subsidies claim that it is unfair for the federal government to subsidize business travelers, who make up a substantial share of Amtrak passengers in congested corridors, and vacationers with high incomes.

Opponents of cutting subsidies say that reducing federal support would lead Amtrak to cancel service on lightly traveled routes and that passengers in those areas might not have alternative transportation available. They also note that subsidizing rail service in congested areas may be justified as a way of offsetting the congestion costs imposed on and by users of highways, airports, and airways. Retaining federal subsidies for Amtrak, especially for congested corridors, may help to redress that imbalance. Moreover, improving service on some corridors could strengthen the national passenger rail system by providing linkages to better-performing routes.

400-02 Eliminate the Essential Air Service Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	50	30
2002	50	50
2003	50	50
2004	50	50
2005	50	50
2001-2005	250	230
2001-2010	500	480

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

300-14

The Essential Air Service (EAS) program was created by the Airline Deregulation Act of 1978 to continue air service to communities that had received federally mandated air service before deregulation. The program provides subsidies to air carriers serving small communities that meet certain criteria. Subsidies currently support air service to about 105 U.S. communities, including 29 in Alaska (for which separate rules apply). The number of passengers served annually has fluctuated in recent years, as has the subsidy per passenger, which has ranged from $4 to $400. The Congress has directed that such subsidies not exceed $200 per passenger unless the community is more than 210 miles from the nearest large or medium-sized hub airport.

This option would eliminate the EAS program, thus providing savings in mandatory outlays of $480 million from 2001 to 2010. To adopt this option, the Congress would have to modify the provision of the Federal Aviation Administration Reauthorization Act of 1996 that authorized $50 million a year in direct spending for the EAS program. That law also authorized the Federal Aviation Administration (FAA) to collect up to $100 million in fees for specified air traffic control services (for certain aircraft flying over the United States but not taking off or landing at a U.S. airport), of which $50 million was to be made available for the EAS subsidies. The law further provided that even if the FAA did not collect $50 million in fees, it still had to provide that amount for the EAS program. The FAA's initial fee structure was overturned in court, however. While the agency is developing a new fee structure, it is collecting no fees. This option would not affect fee collection, but it would sever the link between fees and EAS subsidies. Phasing out the program over several years would mitigate disruptions.

Critics of the EAS program contend that the subsidies are excessive, providing air transportation at a high cost per passenger. They also maintain that the program was intended to be transitional and that the time has come to phase it out. If states or communities derive benefits from service to small communities, the states or communities could provide the subsidies themselves.

Supporters of the subsidy program claim that it prevents the isolation of rural communities that would not otherwise receive air service. Subsidies are not available for service to communities located less than 70 miles from a large or medium-sized hub airport (except in Alaska and Hawaii). The availability of airline transportation is an important ingredient in the economic development of small communities. Without continued air service, according to some proponents, some towns might lose a sizable portion of their economic base.

400-03 Establish Charges for Airport Takeoff and Landing Slots

	Added Receipts (Millions of dollars)
2001	500
2002	500
2003	500
2004	500
2005	500
2001-2005	2,500
2001-2010	5,000

SPENDING CATEGORY:

This fee could be classified as a discretionary offsetting collection or a mandatory offsetting receipt depending on the specific language of the legislation establishing the fee.

RELATED OPTION:

300-07

RELATED CBO PUBLICATION:

Paying for Highways, Airways, and Waterways: How Can Users Be Charged? (Study), May 1992.

In 1968, the Federal Aviation Administration (FAA) established controls on airport takeoff and landing slots at four airports—Kennedy International and La Guardia in New York, O'Hare in Chicago, and Ronald Reagan Washington National Airport—and allocated them to airlines without charge. Airlines are allowed to buy and sell slots from and to each other, with the understanding that the FAA retains ultimate control and can withdraw the slots or otherwise change the rules for using them at any time. Under this option, the FAA would charge annual fees for slots at those airports.

Estimating the revenue from charges for the slots is difficult under any circumstances because slot values vary by airport, time of day and season, and market conditions. Recent legislative and administrative actions have increased uncertainty about slot policies and prices. In 1999, both the Senate and the House of Representatives passed bills to lift restrictions on the slots. Both bills would eliminate slot restrictions at Kennedy and LaGuardia as of January 1, 2007, and would allow interim increases in slots for regional jets serving small hub and nonhub airports. At O'Hare, the House would begin phasing out restrictions in March 2000 and would eliminate them in March 2002. The Senate would phase in 30 additional slots at O'Hare over a three-year period. At Washington National, the Senate would allow 24 additional slots per day; the House would allow six. This year, the Congress will resume its consideration of slot restrictions. If it eliminates them, the value of the slots would eventually reach zero. However, as long as the economy remains strong and the demand for air travel is great, airlines will continue to place a high value on slots that enable them to provide profitable service. CBO estimates receipts to be about $500 million annually, but they could be higher or lower depending on the structure of the slots' leasing arrangements—such as length, whether slots could be subleased, and usage requirements—as well as market conditions affecting the airline industry.

The main argument for establishing charges for slots is that public airspace is scarce and private firms and individuals should pay for the benefits that result from that scarcity. Furthermore, the charges would provide an incentive for using those scarce resources most efficiently.

The main argument against charging for slots is that the scarcity of slots at the four airports mentioned arises mainly from a lack of land and runway space; the fees are not intended to provide more capacity. Furthermore, if the current prices that airlines already pay in the private sale of slots accurately reflect their value, the proposal might not produce more efficient use of those scarce resources; the result would only redistribute the benefits from their use between the private and public sectors.

400-04 Increase User Fees for FAA Certificates and Registrations

	Added Receipts (Millions of dollars)
2001	4
2002	4
2003	4
2004	4
2005	4
2001-2005	20
2001-2010	40

SPENDING CATEGORY:

This fee could be classified as a discretionary offsetting collection or a mandatory offsetting receipt depending on the specific language of the legislation establishing the fee.

RELATED OPTIONS:

300-10, 300-12, and 400-05

The Federal Aviation Administration (FAA) oversees a large regulatory program to ensure safe operation of aircraft within the United States. It oversees and regulates the registration of aircraft, licensing of pilots, issuance of medical certificates, and other similar activities. The FAA issues most licenses and certificates free of charge or at a price well below its cost of providing such regulatory approvals. For example, the current fee for registering aircraft is $5, but the FAA's cost of providing the service is closer to $30. The FAA estimates the cost of issuing a pilot's certificate to be $10 to $15, but the agency does not charge for the certificates. Imposing fees to cover the costs of the FAA's regulatory services could increase receipts by an estimated $20 million over the 2001-2005 period. Net savings could be somewhat smaller than those shown if the FAA needed additional resources to develop and administer fees.

The Drug Enforcement Assistance Act of 1988 authorizes the FAA to impose several registration fees as long as they do not exceed the agency's cost of providing that service. For general aviation, the act allows fees of up to $25 for aircraft registration and up to $12 for pilots' certificates (plus adjustments for inflation). Setting higher fees would require additional legislation. The Congress could provide for them in the legislation currently under consideration that would reauthorize the FAA.

Increasing regulatory fees might burden some aircraft owners and operators. That effect could be mitigated by setting registration fees according to the size or value of the aircraft rather than to the FAA's cost. FAA fees based on the cost of service, however, would be comparable with automobile registration fees and operators' licenses and thus are likely to be affordable, especially when compared with the total cost of owning an airplane.

400-05 Establish Marginal Cost-Based Fees for Air Traffic Control Services

	Added Receipts (Millions of dollars)
2001	2,000
2002	2,000
2003	2,000
2004	2,000
2005	2,000
2001-2005	10,000
2001-2010	20,000

SPENDING CATEGORY:

This fee could be classified as a discretionary offsetting collection or a mandatory offsetting receipt depending on the specific language of the legislation establishing the fee.

RELATED OPTIONS:

300-10, 300-12, 400-05, and 400-06

RELATED CBO PUBLICATION:

Paying for Highways, Airways, and Waterways: How Can Users Be Charged? (Study), May 1992.

The Federal Aviation Administration (FAA) operates the air traffic control (ATC) system, which serves commercial air carriers, military aircraft, and such smaller users as air taxis and private corporate and recreational aircraft. Traffic controllers in airport towers, terminal radar approach control facilities (TRACONs), and air route traffic control centers (ARTCCs) help guide aircraft safely as they taxi to the runway, take off, fly through designated airspace, land, and taxi to the airport gate. Other ATC services include flight service stations that provide weather data and other information useful to small-aircraft operators.

This option would impose fees for ATC services that reflect the FAA's marginal costs of providing the services. The marginal cost of a flight equals the costs of each ATC service (or contact) provided for that flight. For example, a commercial flight from New York to San Francisco entails contacts with two airport towers, two TRACONs, and seven ARTCCs. Under this option, the airline would pay the sum of the marginal costs of each of those contacts. A 1997 FAA study estimated total marginal costs to be about $2 billion a year.

Fees based on marginal costs would affect different types of airline operations differently. Carriers mainly using hub-and-spoke networks would probably face higher fees than those providing nonstop origin-destination flights because of differences in the number of contacts with towers and TRACONs.

Imposing fees for marginal costs would encourage users to use the ATC system efficiently. Noncommercial users might reduce their consumption of ATC services, freeing controllers for other tasks and increasing the system's overall capacity. By analyzing the pattern of revenues from user fees, FAA planners could better decide on the amount and location of additional ATC investment, which would make the system more efficient.

The main argument against this option is that it would raise the cost of ATC services to users. Such a move could weaken the financial condition of some commercial air carriers.

400-06 Impose a User Fee to Cover the Cost of the Federal Railroad Administration's Rail Safety Activities

	Added Receipts (Millions of dollars)
2001	77
2002	77
2003	77
2004	77
2005	77
2001-2005	385
2001-2010	770

SPENDING CATEGORY:

This fee could be classified as a discretionary offsetting collection or a mandatory offsetting receipt depending on the specific language of the legislation establishing the fee.

RELATED OPTIONS:

300-10, 300-12, 400-04, and 400-05

The function of the Federal Railroad Administration's (FRA's) rail safety activities is to protect railroad employees and the public by ensuring the safe operation of passenger and freight trains. Field safety inspectors are responsible for enforcing federal safety regulations and standards. Other functions include issuing standards, procedures, and regulations; administering postaccident and random drug testing of railroad employees; providing technical training; and managing highway grade-crossing projects.

Railroad safety fees, which had been authorized in the Omnibus Budget Reconciliation Act of 1990, expired in 1995. Before 1995, railroads were subject to the FRA's safety oversight user fees that covered the safety enforcement and administrative costs of carrying out FRA's mandated safety responsibilities. Those fees offset a portion of federal spending on safety programs. Since this authority expired in 1995, FRA has not assessed user fees for operating its safety program.

This option would impose new user fees to offset the costs of the FRA's rail safety activities—$700 million over 10 years. Those in favor of user fees contend that the specific recipients of government services should bear the cost of those services. The user fees would relieve the general taxpayer of the burden of supporting the FRA's rail safety activities.

People who oppose having users pay for the service contend that the general public is the main beneficiary of the FRA's rail safety activities. Critics of this option also note that other than businesses in the pipeline industry, no other freight or transportation businesses pay safety user fees.

450

Community and Regional Development

Budget function 450 includes programs that support the development of physical and financial infrastructure intended to promote viable community economies, including activities of the Department of Commerce and the Department of Housing and Urban Development. This function also includes spending to help communities and families recover from natural disasters and spending for the rural development activities of the Department of Agriculture, the Bureau of Indian Affairs, and other agencies. CBO estimates that in 2000, discretionary outlays for function 450 will be $11.4 billion. Over the past decade, spending for community and regional development has increased in most years.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	7.3	5.8	11.3	9.6	15.3	12.0	11.6	13.0	10.3	11.0	11.4
Outlays											
Discretionary	7.3	6.1	6.4	8.4	10.8	10.1	10.4	10.7	10.1	11.9	11.4
Mandatory	1.3	0.7	0.5	0.8	-0.2	0.6	0.4	0.4	-0.4	0	-0.7
Total	8.5	6.8	6.8	9.2	10.6	10.7	10.7	11.1	9.8	11.9	10.7
Memorandum:											
Annual Percentage Change in Discretionary Outlays		-16.1	4.0	32.0	29.0	-6.3	2.2	3.1	-5.3	17.4	-4.1

450-01 Convert the Rural Community Advancement Program to State Revolving Loan Funds

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	0	0
2002	0	0
2003	0	0
2004	0	0
2005	0	0
2001-2005	0	0
2001-2010	3,595	1,683
Relative to WIDI		
2001	0	0
2002	0	0
2003	0	0
2004	0	0
2005	0	0
2001-2005	0	0
2001-2010	4,111	1,893

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

270-05 and 300-03

The Department of Agriculture's Rural Community Advancement Program (RCAP) assists rural communities by providing loans, loan guarantees, and grants for rural water and waste disposal projects, community facilities, economic development, and fire protection. Funds are generally allocated among the states on the basis of their rural populations and the number of rural families with income below the poverty threshold. Within each state's allocation, the department awards funds competitively to eligible applicants, including state and local agencies, nonprofit organizations, and (in the case of loan guarantees for business and industry) for-profit firms.

The terms of a particular recipient's assistance depend on the purpose of the aid and, in some cases, the economic condition of the recipient's area. For example, aid for water and waste-disposal projects can take the form of loans with interest rates ranging from 4.5 percent to market rates, depending on the area's median household income; areas that are particularly needy may receive grants or a mix of grants and loans.

For 2000, the Congress appropriated $719 million for RCAP's grants and the budgetary cost of its loans and loan guarantees, which is defined under credit reform as the present value of the interest rate subsidies and expected defaults. The Congress could reduce future spending by capitalizing state revolving loan funds (SRLFs) for rural development and then ending federal RCAP assistance. The amount of federal savings would depend on the level and timing of the contribution to capitalize the SRLFs. Under one illustrative option, the federal government would provide steady funding of $719 million annually for five more years to capitalize the funds, then cut off assistance in 2005. The option would yield savings of $1.7 billion from 2006 to 2010. That level of capitalization alone would not support the volume of loans and grants now provided annually by RCAP. Accordingly, the Congress could choose to allow the SRLFs to use the capitalization funds as collateral with which to leverage additional capital from the private sector, as has been allowed with the SRLFs established under the Clean Water Act and Safe Drinking Water Act.

The main argument for replacing RCAP with a system of SRLFs is that the federal government should not bear continuing responsibility for local development; rather, programs that benefit localities, whether urban or rural, should be funded at the state or local level. On the basis of that argument, a few more years of federal funding to capitalize SRLFs would provide a reasonable transition to the desired policy.

One argument against converting RCAP is that without annual infusions of new federal money, states will feel a need to stretch their rural development funds by reducing the number of grants and interest rate subsidies, making it harder for needier communities to find affordable assistance. In addition, precedent suggests that the estimated federal savings may not materialize: the Congress continues to appropriate additional grants to the state funds for wastewater treatment systems, long past the point at which those funds were originally designed to be independent of federal support.

450-02 Eliminate the Appalachian Regional Commission

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	66	7
2002	66	20
2003	66	40
2004	66	51
2005	66	59
2001-2005	330	177
2001-2010	660	507
Relative to WIDI		
2001	67	7
2002	68	20
2003	69	41
2004	71	53
2005	72	62
2001-2005	347	183
2001-2010	725	546

SPENDING CATEGORY:

Discretionary

The federal government provides annual funding to the Appalachian Regional Commission (ARC) for activities that promote economic growth in the Appalachian counties of 13 states. For 2000, the Congress appropriated $66 million for ARC. The states are responsible for filing development plans and recommending specific projects for federal funding. The commission distributes the funds competitively according to such factors as the area's growth potential, per capita income, and unemployment rate; the financial resources of the state and locality; the project's prospective long-term effectiveness; and the degree of private-sector involvement.

ARC supports a variety of programs, including the Community Development Program, mainly to create jobs; the Human Development Program, to improve rural education and health; and the Local Development District Programs, to provide planning and technical assistance to multicounty organizations. (In 1998, the Congress transferred the responsibility for the Appalachian Development Highway System, previously another main ARC program, to the general Transportation Trust Fund.) Federal funds also support 50 percent of the salaries and expenses of ARC staff. Discontinuing the programs funded through ARC would reduce federal outlays by $7 million in 2001 and by $507 million over the 2001-2010 period.

The debate over eliminating ARC focuses on two main points. First, ARC's critics argue that the responsibility for supporting local or regional development basically lies with the state and local governments whose citizens will benefit from the development, not with the federal government. ARC's supporters believe that the federal government has a legitimate role to play in redistributing funds among states to support development in the neediest areas and that reducing federal funding would reduce local progress in job creation, education, and health care. Second, the agency's critics note that all parts of the country have needy areas and argue that those areas in Appalachia have no special claim to federal dollars. According to such critics, needy Appalachian areas should, like other areas, get federal development aid through national programs, such as those of the Economic Development Administration. ARC's defenders respond that Appalachia's size, physical isolation, and severe poverty have created a unique situation requiring special attention.

450-03 Drop Wealthier Communities from the Community Development Block Grant Program

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	593	12
2002	593	202
2003	593	451
2004	593	534
2005	593	563
2001-2005	2,965	1,762
2001-2010	5,930	4,721
Relative to WIDI		
2001	605	12
2002	615	206
2003	626	463
2004	636	556
2005	647	594
2001-2005	3,129	1,831
2001-2010	6,532	5,099

SPENDING CATEGORY:

Discretionary

The Community Development Block Grant (CDBG) program provides annual grants, by formula, to metropolitan cities and urban counties through what is referred to as its entitlement component. The program also allocates funds, by formula, to each state. Those funds are distributed among the states' smaller and more rural communities, called nonentitlement areas, typically through a competitive process.

In general, CDBG funds must be used to aid low- and moderate-income households, eliminate slums and blight, or meet emergency needs. Specific eligible uses include housing rehabilitation, infrastructure improvement, and economic development. Funds from the entitlement component may also be used to repay bonds that are issued by local governments (for acquiring public property, for example) and guaranteed by the federal government under the Section 108 program. For 2000, the CDBG program received a regular appropriation of $4.8 billion, including $3.0 billion for entitlement communities.

Under current law, all urban counties, metropolitan cities, and other cities of 50,000 or more are eligible for the CDBG entitlement program. The formula for allocating entitlement funds includes the following factors: population, the number of residents with income below the poverty level, the number of housing units with more than one person per room, the number of housing units built before 1940, and the extent to which an area's population growth since 1960 is less than the average for all metropolitan cities. The formula neither requires a threshold percentage of residents living in poverty nor excludes communities with high average income.

Federal spending for the program could be reduced by focusing entitlement grants on more needy jurisdictions and lowering funding accordingly. Several alternative changes to the current formula could yield similar results; one simple approach, however, would be to exclude communities whose per capita income exceeds the national average by more than a certain percentage. Data from the Department of Housing and Urban Development on the 1993 grants to entitlement cities (but not counties) suggest that restricting the grants to communities whose per capita income is less than 112 percent of the national average, for example, would save 26 percent of the entitlement funds, in part by cutting the large grants to New York City and Los Angeles. To illustrate the general idea, the Congressional Budget Office has assumed a somewhat smaller cut of 20 percent of entitlement funding, which would save an estimated $12 million in 2001 and $4.7 billion from 2001 to 2010.

Proponents of that change argue that if the CDBG program can be justified at all—some argue that using federal funds for local development is generally inappropriate—its primary rationale is redistribution and that redistributing money to less needy communities serves no pressing interest. Opponents argue that such a change would reduce efforts to aid low- and moderate-income households in poverty pockets within those communities because local governments would not sufficiently redirect their own funds to completely offset the lost grants.

450-04 Eliminate the Neighborhood Reinvestment Corporation

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	75	75
2002	75	75
2003	75	75
2004	75	75
2005	75	75
2001-2005	375	375
2001-2010	750	750
Relative to WIDI		
2001	76	76
2002	77	77
2003	79	79
2004	80	80
2005	82	82
2001-2005	394	394
2001-2010	823	823

SPENDING CATEGORY:

Discretionary

The Neighborhood Reinvestment Corporation (NRC) is a public, nonprofit organization charged with revitalizing distressed neighborhoods. The NRC oversees a network of locally initiated and operated groups called NeighborWorks® organizations, or NWOs, which engage in a variety of housing, neighborhood revitalization, and community-building activities. The corporation provides technical and financial assistance to begin new NWOs; it also monitors and assists current network members. As of 1998, the NeighborWorks® network had 181 members operating in 825 communities nationwide.

For 2000, the NRC's appropriation is $75 million. With those funds, plus a few million dollars from fees and other sources, the corporation provides grants, conducts training programs and educational forums, and produces publications in support of member NWOs. The bulk of the grant money goes to NWOs, which use the funds to cover operating costs; conduct projects; purchase, construct, and rehabilitate properties; and capitalize their revolving loan funds. NWO revolving loan funds make home ownership and home improvement loans to individuals or loans to owners of mixed-use properties who provide long-term rental housing for low- and moderate-income households. In addition, the NRC awards grants to Neighborhood Housing Services of America to provide a secondary market for the loans from NWOs. Eliminating the NRC would save $750 million over 10 years.

One argument for eliminating the NRC is that the federal government should not fund programs whose benefits are local rather than national. A second argument is that the NeighborWorks® approach duplicates the efforts of programs from other federal agencies (particularly the Department of Housing and Urban Development, or HUD) that also rehabilitate low-income housing and promote home ownership and community development. Third, critics of the corporation argue that even within the NeighborWorks® approach, the NRC is a redundant funding channel. In 1997, NRC grants accounted for about one-quarter of the NWOs' governmental funding and roughly 6 percent of their total funding. Larger shares came from private lenders, foundations, corporations, and HUD.

The NRC's defenders argue that the large number of federal programs to assist local development is evidence of widespread support for a federal role—particularly in areas where state and local governments may lack adequate resources of their own. They further argue that NWOs focus on whole neighborhoods rather than individual housing properties, and with their nonhousing activities—such as community organization building, neighborhood cleanup and beautification, and leadership development—provide economic and social benefits that other federal programs do not. Finally, defenders say that the NRC is a valuable part of the approach because of its flexibility in making grants, which allows it to fund valuable NWO efforts that do not fit within the narrow criteria of larger federal grantors, and the services it provides to the NWOs, such as training, program evaluation, and technical assistance.

450-05 Drop Flood Insurance for Certain Repeatedly Flooded Properties

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	58
2002	0	62
2003	0	67
2004	0	72
2005	0	77
2001-2005	0	336
2001-2010	0	822

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

450-06

Data from the National Flood Insurance Program (NFIP) show that a relatively small number of properties subject to repeated flooding account for a large share of the losses incurred by the program. The Federal Emergency Management Agency (FEMA), which administers the NFIP, has focused its attention on properties that have incurred two or more losses of at least $1,000 each in any 10-year period since 1978 (the earliest year for which data are available). The more than 87,000 properties fitting that definition account for about one-third of all claims, by both number and dollar value, since 1978. Many of those properties no longer have flood insurance: in some cases, the property has been destroyed or moved; in other cases, the owner dropped the policy—for example, after FEMA limited coverage under the NFIP for basement losses in 1983. The NFIP currently insures roughly 43,000 repeatedly flooded properties, representing about 1 percent of all policies in force but a much larger share of annual flood losses.

The issue of repeatedly flooded properties raises concern in part because they generally are covered at premium rates that do not adequately reflect their risk of flood losses. FEMA data show that 95 percent of such properties were built before the development of the Flood Insurance Rate Map (FIRM) for their respective communities—which is not surprising, given the flood mitigation requirements imposed on post-FIRM construction. Thus, almost all repeatedly flooded properties are covered under the pre-FIRM premium rates that the government explicitly subsidizes. (See the related discussion for option 450-06.) In addition, although some properties may incur losses twice in 10 years because of a bad "draw" of storms or other random events, others have flooded four, five, or even 10 or 20 times since 1978, demonstrating that the gap between the pre-FIRM rates and their true actuarial risk of flood loss is particularly large.

One way to reduce federal costs for the flood insurance program would be to deny coverage after the fourth loss of at least $1,000 in any 20-year period. FEMA data indicate that the option would immediately affect about 8,800 properties, and the Congressional Budget Office estimates that it would reduce federal outlays by $58 million in 2001 and $822 million over the 2001-2010 period. The main argument for the option is that neither taxpayers nor other policyholders should be required to provide an unlimited subsidy for properties known to be at high risk for frequent flood damage. The loss or threat of losing NFIP protection would encourage owners of such properties to take appropriate mitigation measures, such as elevating their structures or rebuilding elsewhere.

Opponents of dropping the flood insurance argue that it would be unfair to the property owners to suddenly withdraw their protection from flood risk—especially owners who have occupied their properties since before the local FIRM was developed and cannot readily afford relocation or other costly mitigation measures. Some opponents might prefer a more moderate change from current policy, such as adding a repetitive-loss surcharge to insurance premiums or denying coverage only to policyholders who reject offers of mitigation assistance.

450-06 Reduce the Flood Insurance Subsidy on Pre-FIRM Structures

	Net Receipts (Millions of dollars)
2001	25
2002	81
2003	113
2004	120
2005	137
2001-2005	466
2001-2010	1,185

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

450-05

The National Flood Insurance Program (NFIP) charges two different sets of premiums: one for "pre-FIRM" buildings constructed before 1975 or before the completion of a participating community's Flood Insurance Rate Map (FIRM), and another for post-FIRM buildings. Post-FIRM premiums are intended to be actuarially sound —that is, to cover the costs of all insured losses over the long term—and are based on buildings' elevations relative to the water level expected during a flood that is predicted to occur less than once every 100 years. In contrast, pre-FIRM rates are heavily subsidized, on average, and do not take elevation into account. Currently, about one-sixth of all flood insurance coverage is provided at pre-FIRM rates.

The Federal Emergency Management Agency (FEMA), which administers the flood insurance program, estimates that 31 percent of current policyholders are paying pre-FIRM rates. Those rates are available only for the first $35,000 of coverage for a single-family or a two- to four-family dwelling and for the first $100,000 of coverage for a larger residential, nonresidential, or small business building. Various levels of additional coverage are available at actuarially neutral rates. The program also offers insurance for buildings' contents; again, policyholders in pre-FIRM buildings pay lower rates for a first tier of coverage. The Congressional Budget Office estimates that on average, the first-tier prices represent 38 percent of the coverages' actuarial value, implying a subsidy rate of 62 percent. The size of the subsidy for any particular building depends heavily on its elevation. For buildings that lie above the 100-year-flood level, post-FIRM premiums are actually lower than the "subsidized" pre-FIRM rates. Owners of such properties can reduce their insurance costs by getting the elevation certified, and many have done so.

Reducing the average subsidy from 62 percent to 50 percent—implying a premium increase of about 30 percent in the subsidized tier—would yield net new receipts of $25 million in 2001 and $1.2 billion over the 2001-2010 period. Those estimates take into account the likelihood that some current policyholders would drop their coverage. Flood insurance is mandatory only for properties in special flood hazard areas that carry mortgages from federally insured lenders, and compliance with the requirement is far from complete. Accordingly, CBO expects that the proposal would somewhat reduce the participation of both voluntary and mandatory purchasers.

Advocates of the proposal argue that the subsidy has outlived its original justification as a temporary measure to encourage participation among property owners who were not previously aware of the magnitude of the flood risks they faced. Raising premiums closer to actuarial levels, such advocates maintain, would make policyholders pay more of their fair share for insurance protection and would give them stronger incentives to relocate or take preventive measures.

Supporters of the current subsidy contend that a 30 percent increase in premiums would be an unfair burden to owners of pre-FIRM properties, which were built before FEMA documented the extent of the flood hazards, and that the increase would be particularly unjust for those policyholders who are already paying a negative "subsidy" (because they are unaware that their properties lie above the 100-year-flood elevation). Subsidy supporters further argue that reduced rates of participation in the program would lead to increased spending on disaster grants and loans and thereby erode some of the savings projected for the option. Finally, they question the accuracy of the maps FEMA uses to estimate the average long-run subsidy, noting that for most pre-FIRM properties except a relatively few structures that repeatedly flood, premiums now roughly equal the average losses incurred to date.

450-07 Eliminate the Community Development Financial Institutions Fund

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	80	15
2002	94	41
2003	94	71
2004	94	88
2005	94	93
2001-2005	456	308
2001-2010	926	778
Relative to WIDI		
2001	81	15
2002	98	42
2003	99	73
2004	101	92
2005	102	99
2001-2005	481	321
2001-2010	1,022	847

SPENDING CATEGORY:

Discretionary

The Congress created the Community Development Financial Institutions (CDFI) fund in 1994 to expand the availability of credit, investment capital, and financial services in distressed communities. The fund provides equity investments, grants, loans, and technical assistance to CDFIs, which include community development banks, credit unions, loan funds, venture capital funds, and microenterprise funds. In turn, the CDFIs provide a range of financial services—such as mortgage financing for first-time home buyers, loans and investments for new or expanding small businesses, and credit counseling—in market niches underserved by traditional institutions. The CDFI fund also provides incentive grants to traditional banks and thrifts to invest in CDFIs and to increase loans and services to distressed communities.

For 2000, the Congress appropriated $95 million for the CDFI fund. Eliminating the fund would save $778 million over 10 years, taking into account the small amount of spending that would still be required by another agency (perhaps the Small Business Administration) for oversight of the fund's existing loan portfolio.

Opponents criticize the fund on several grounds. First, as with many of the options in this section, some critics argue that local development should be funded at the state or local level, not by the federal government, since its benefits are not national in scope. Second, opponents see the fund as redundant, given that many other federal programs support home ownership and local economic development, including the Empowerment Zones/Enterprise Communities Program, housing loan programs of the Rural Housing Service, Community Development Block Grants, the Neighborhood Reinvestment Corporation, and the Economic Development Administration, among others. Appropriations for those five programs totaled $6 billion in 1999. Third, some critics argue that assistance to CDFIs is likely to be inefficient, encouraging them to make loans that would not pass market tests for creditworthiness. Fourth, opponents say that the fund has been poorly managed: an oversight report from the House Banking Committee found that the fund had not followed accepted federal procedures in making its first round of grants in 1996, had not accurately documented the factors used in selecting applicants, and had paid excessive rates to outside contractors hand-picked by CDFI officials. The fund's director and deputy director resigned in August 1997.

Supporters of the fund argue that the federal government has a legitimate role in assisting needy communities and that the fund provides an efficient mechanism for leveraging private-sector investment with a relatively small federal contribution. They also say that management has improved under the fund's new director, noting that its audit for fiscal year 1998 showed no material weaknesses and that the House Banking Committee reported a bill in 1999 to reauthorize the fund for four years while providing some additional management controls.

500

Education, Training, Employment, and Social Services

Budget function 500 primarily includes federal spending within the Departments of Education, Labor, and Health and Human Services for programs that directly provide—or assist states and localities in providing—services to young people and adults. The activities that it covers include providing developmental services to low-income children, helping disadvantaged and other elementary and secondary school students, offering grants and loans to postsecondary students, and funding job-training and employment services for people of all ages. CBO estimates that total outlays for function 500 will be $63.9 billion in 2000. Discretionary outlays represent $49.8 billion of that total. Over the past decade, function 500 has experienced increases in discretionary spending in all but one year.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	30.0	33.8	36.3	38.2	40.6	39.9	36.5	42.8	46.7	46.6	44.5
Outlays											
Discretionary	27.9	30.6	34.0	36.5	37.6	38.9	38.5	39.6	42.5	45.1	49.8
Mandatory	10.9	12.8	11.2	13.5	8.7	15.3	13.5	13.4	12.4	11.3	14.1
Total	38.8	43.4	45.2	50.0	46.3	54.3	52.0	53.0	55.0	56.4	63.9
Memorandum:											
Annual Percentage Change in Discretionary Outlays		9.8	11.2	7.2	3.1	3.5	-1.2	3.1	7.3	6.1	10.3

500-01 Reduce Funding for Title I, Education for the Disadvantaged

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	87	17
2002	339	271
2003	339	332
2004	339	339
2005	339	339
2001-2005	1,443	1,298
2001-2010	3,137	2,993
Relative to WIDI		
2001	116	23
2002	482	369
2003	594	538
2004	716	664
2005	838	786
2001-2005	2,746	2,380
2001-2010	8,822	8,184

SPENDING CATEGORY:

Discretionary

Title I of the Elementary and Secondary Education Act of 1965 provides two kinds of grants to school districts to fund supplementary educational services for educationally disadvantaged children. Basic grants allocate federal funds on the basis of the number of children who live in families with income below the poverty level in a particular geographic area. Concentration grants provide additional funds to school districts in counties in which the number of poor children exceeds 6,500 or 15 percent of the school-age population. Although Title I distributes funds on the basis of the number of poor students in a district, schools that receive the money may use it to provide services to any students who are performing well below their grade level.

Title I funds reached about 45,000 schools in 1999 and served approximately 10 million children. About 15,000 schools operated schoolwide programs (which benefit all of the children in a specific school), and another 30,000 participated in targeted assistance programs (which must focus the grants on the children most in need of Title I services).

This option would reduce funding for basic grants to local educational agencies by 5 percent, saving $17 million in federal outlays in 2001 and $3 billion over the 2001-2010 period. To direct cuts toward the schools with the least need for Title I services, the eligibility criteria for receiving funding could be altered. Currently, the law restricts Title I basic grant funds to school districts that have 2 percent of their children living in families with income below the poverty level and at least 10 poor children. If the Congress raised the lower bound on the criterion for the percentage of children living in poverty (for example, to 5 percent or 10 percent), funding could be maintained at its current level for the school districts that satisfied the more restrictive eligibility criteria.

Some proponents of eliminating federal funding for elementary and secondary education argue that such support represents federal intervention into matters that are primarily of state and local concern. Opponents, however, insist that federal funding augments state and local efforts and ultimately makes them more successful.

The primary argument for reducing Title I funding in particular is that there is little evidence that it improves the long-term academic performance of students who receive its services. Many studies have compared students receiving Title I services with groups of students that are similar by grade and poverty status. Such studies show that program participants do not improve their academic achievement relative to other students. However, supporters of the program maintain that Title I funds help underachieving students in schools that serve many poor children. Advocates also note that such funding is a major federal instrument for fostering school reform because states applying for the grants must develop standards specifying what public school children should know and be able to do at various points in their education.

500-02 Eliminate Funding for Bilingual Education

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	248	30
2002	248	198
2003	248	243
2004	248	248
2005	248	248
2001-2005	1,240	967
2001-2010	2,480	2,207
Relative to WIDI		
2001	252	30
2002	256	202
2003	261	251
2004	265	260
2005	270	265
2001-2005	1,304	1,008
2001-2010	2,722	2,400

SPENDING CATEGORY:

Discretionary

Federal bilingual education programs authorized under title VII of the Elementary and Secondary Education Act provide grants to school districts for instructing students who have limited proficiency in English (so-called LEP students). School districts use the funds primarily to support bilingual instructional services, to disseminate information on ways to serve students whose English is limited, and to train instructors to teach in bilingual classrooms.

Bilingual education projects funded through title VII provide a range of services to LEP students. Most schools use English as a Second Language projects to meet those students' needs. In the projects, teachers instruct children jointly in English and their native language but stress a rapid grasp of English. No more than 25 percent of federal funding for bilingual education programs may be used to support instruction conducted only in English.

Eliminating federal funding for bilingual education programs under title VII would reduce federal outlays by $30 million in 2001 and $2.2 billion over the 2001-2010 period.

Supporters of this option contend that bilingual education programs under title VII do not effectively advance literacy in the English language and slow the integration of LEP students into regular classrooms. They maintain that the federal government should not fund programs requiring the use of a student's native language but should encourage school districts to move LEP students into regular classrooms as quickly as possible. Many supporters of this option argue that "immersion" programs, in which LEP students are instructed solely in English, are the most effective means to teach English to such students.

Defenders of bilingual education assert that it serves a valuable purpose. By introducing students to the English language while continuing instruction in their native language, the program helps students acquire knowledge in a variety of academic subjects as they develop their English literacy skills. As a result, supporters argue, students do not fall behind their schoolmates in other subjects during their transition to English-only instruction.

500-03 Reduce Funding to School Districts for Impact Aid

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	73	66
2002	73	71
2003	73	73
2004	73	73
2005	73	73
2001-2005	364	356
2001-2010	729	720
Relative to WIDI		
2001	74	67
2002	75	74
2003	77	76
2004	78	78
2005	79	79
2001-2005	383	373
2001-2010	799	789

SPENDING CATEGORY:

Discretionary

The Impact Aid program, authorized under title VIII of the Elementary and Secondary Education Act, provides funds to school districts affected by activities of the federal government. The program pays districts for federally connected pupils and for school construction in areas where the federal government has acquired a significant portion of the real property tax base, thereby depriving the school district of a source of revenue.

For a school district to be eligible for Impact Aid's basic support payments, a minimum of 3 percent (or at least 400) of its pupils must be associated with activities of the federal government—for example, pupils whose parents both live and work on federal property (including Indian lands), pupils whose parents are in the uniformed services but live on private property, and pupils who live in federally subsidized low-rent housing. In addition, aid goes to a few districts enrolling at least 1,000 pupils (and 10 percent of enrollment) whose parents work but do not live on federal property. In 1999, approximately 1,500 local education agencies received Impact Aid.

This option would restrict Impact Aid to the school districts that are most affected by federal activities—districts with children who live on federal property and have a parent who is in the military or is a civilian federal employee and districts with children who live on Indian lands. The restriction would reduce federal outlays by $720 million during the 2001-2010 period. The Administration's budget for fiscal year 2000 included this option in its list of recommendations.

Proponents of this alternative argue that restricting Impact Aid payments to students whose presence puts the greatest burden on school districts is appropriate, given the limited funding available for federal discretionary programs. Opponents argue that eliminating payments for other types of children associated with federal activities could significantly affect certain districts—for example, those in which large numbers of military families live off-base but shop at military exchanges, which do not collect state and local sales taxes.

500-04 Limit Federal Funding for State Education Reform

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	88	7
2002	131	73
2003	131	117
2004	131	127
2005	131	130
2001-2005	611	453
2001-2010	1,264	1,106
Relative to WIDI		
2001	98	204
2002	155	278
2003	170	188
2004	186	183
2005	201	187
2001-2005	810	1,039
2001-2010	2,060	2,191

SPENDING CATEGORY:

Discretionary

The federal government currently supports education reform at the state and local levels through two programs that have related purposes but quite different structures. The first program, the Innovative Education Program Strategies (IEPS) state grants (authorized under title VI of the Elementary and Secondary Education Act), provides relatively untargeted funding in the form of block grants to supplement state and local funding for elementary and secondary education reform. Recipients may use funds from the grants to carry out programs in a number of broad categories, but those activities need not be tied to any specific reform plan or set of standards.

In contrast, funds under Goals 2000 may only be used to pursue a systemic model of reform, which involves setting goals and standards for reform, developing benchmarks to promote progress toward the goals, and pursuing reform at all levels of the education system. Activities that are consistent with that model include developing state standards for reform, aligning local curricula with those standards, paying for professional development activities for teachers and other staff, and purchasing technology.

Reducing federal funding for education reform activities now funded under IEPS state grants and Goals 2000 by 15 percent would cut federal outlays by $7 million in 2001 and $1.1 billion over the 2001-2010 period. Lawmakers could retain the current relative distribution of funding between the two types of approaches or shift funding to favor one approach or the other.

Proponents of decreasing federal funding for both types of education reform argue that state and local governments are already carrying out school reforms on their own and do not need additional federal support. Federal funding for education reform is unnecessary, say those proponents, and constitutes needless federal intervention into matters that are primarily of state and local concern. Opponents of limiting federal support insist that federal funds augment ongoing state and local reform efforts and contribute to their faster and more complete implementation.

Among supporters of some federal role in education reform, opinions differ about which type of program should receive the larger share of federal funding. Proponents of more funding for the activities currently supported under the Goals 2000 program argue that those activities are better designed to foster systemic reform. Because Goals 2000 links funding to a state reform plan, supporters maintain that the funds are better directed and have a greater impact on the quality of schools within a state. In contrast, supporters of the title VI block grants insist that those grants are a better tool for supplementing state education reform. By offering greater flexibility, supporters say, block grants allow states to fund the local reforms that are best suited to particular communities—even if those reforms are not tied to a larger state effort.

500-05 Eliminate Funding for Federal Initiatives to Reduce Class Size

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	400	65
2002	1,300	910
2003	1,300	1,235
2004	1,300	1,300
2005	1,300	1,300
2001-2005	5,600	4,810
2001-2010	12,100	11,310
Relative to WIDI		
2001	407	66
2002	1,329	927
2003	1,350	1,272
2004	1,374	1,359
2005	1,397	1,383
2001-2005	5,856	5,006
2001-2010	13,202	12,279

SPENDING CATEGORY:

Discretionary

For fiscal year 2000, the Congress appropriated $1.3 billion to reduce the size of elementary school classes nationwide. The law also allows school districts to use up to 25 percent of local grants to improve teacher quality. Moreover, districts in which class sizes have already been reduced can use the funds to improve the quality of teachers in the lower grades or to hire more teachers for upper grades. By eliminating funding for the program, the federal government could save $11.3 billion in outlays over the next 10 years.

In recent reviews of the scientific evidence for the benefits of small classes, the results of one study, Tennessee's Project STAR, are prominent because of the study's rigorous experimental design. Children entering kindergarten were randomly assigned either to special small classes of between 13 and 17 students or to "regular" classes of between 22 and 26 students. With only few exceptions, students remained in the same size class to which they were initially assigned through the end of the third grade.

Testing showed that students in the small classes outperformed students in the regular classes on both standardized and curriculum-based tests. In the early grades, the positive effect of small classes on achievement among minority students was twice that for nonminority students. Through eighth grade, students who had been in the small classes showed a decreasing but still significantly higher level of academic achievement than students in the regular classes.

Proponents of eliminating federal funding for class-size initiatives see limitations to Project STAR's success. If education is cumulative, with each year building on what was learned the year before, children assigned to a small class would be expected to pull further away from their counterparts in a regular class for each year they remained in the small class. In fact, the evidence shows such advances for youngsters in small classes only at the end of kindergarten and, to a lesser extent, at the end of first grade. Critics of a policy advocating small class sizes also point to other evidence suggesting that class size must fall to about 15 students before it has an effect. Reducing class sizes to those levels would be quite expensive, and the costs would increase over time. More classrooms would have to be built; new teachers would require services such as staff training; and as they gained experience, those teachers' salaries would increase. Finally, the critics note that strategies such as providing one-on-one or peer tutoring as well as cooperative learning achieve results similar to those gained from reducing class size—but at a fraction of the cost.

Supporters of funding for initiatives to decrease class sizes find that approach attractive because it moves resources directly to the classroom and to students. Furthermore, many analysts have concluded that enrollment in the early grades in small classes of about 18 or fewer students can have positive effects on a student's academic achievement, compared with enrollment in classes of between 25 and 30 students. Minority students in particular seem to benefit from small classes. In addition, most of the benefits students gain from being in a small class appear to persist into later grades.

500-06 Consolidate and Reduce Funding for Several Elementary and Secondary Education Programs

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	328	24
2002	479	291
2003	479	438
2004	479	471
2005	479	478
2001-2005	2,246	1,702
2001-2010	4,643	4,099
Relative to WIDI		
2001	384	28
2002	613	345
2003	697	563
2004	783	677
2005	869	770
2001-2005	3,346	2,383
2001-2010	2,963	2,355

SPENDING CATEGORY:

Discretionary

Current federal programs to aid elementary and secondary education are generally categorical—that is, they focus on specific populations of students with special needs (for example, disabled students or educationally disadvantaged students), on subject areas of high priority to policymakers (such as mathematics or science), or on specific approaches to improving education (for instance, charter schools). The Congress adopted categorical forms of federal aid in certain cases because of a belief that many states would be unable or unwilling to commit funds to those priorities. Categorical programs focusing on education reform and school innovation, for which the Congress appropriated a combined $4.8 billion in fiscal year 2000, could be consolidated under a single block grant. Funds from the grant could be used for any of the purposes previously authorized for the categorical programs.

To reduce federal outlays, the federal government could trim the consolidated block grant for education reform and school innovation by, for example, 10 percent. Doing so would save $24 million in 2001 and $4.1 billion over 10 years.

Proponents of block grants for education point out that they give states and local education agencies the flexibility to direct federal aid toward the schools' greatest needs. Block grants can circumvent the administrative requirements accompanying categorical aid programs, which may limit a school's ability to implement comprehensive reforms. Block grants also avoid the problems created within a school by a proliferation of categorical programs that may lead to gaps in a child's instructional program in some areas and duplication in others. Moreover, by requiring that funds be clearly associated with the intended beneficiaries, categorical grants may encourage schools to partially segregate children with special needs, track students by achievement level, or perpetuate lower expectations of their performance.

Opponents of education block grants argue that they dilute the effect of federal funding on national educational priorities and provide less assurance than categorical funding that federal aid will be used to meet national objectives. Moreover, opponents point out that alternative means, such as waivers, are now available to give state and local education agencies increased flexibility in using funds from categorical programs without sacrificing federal priorities.

500-07 Reduce Spending and Increase the Targeting of Funds for Safe and Drug Free Schools and Communities

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	41	5
2002	91	64
2003	91	86
2004	91	91
2005	91	91
2001-2005	405	336
2001-2010	859	791
Relative to WIDI		
2001	46	5
2002	106	71
2003	116	103
2004	127	119
2005	138	129
2001-2005	532	428
2001-2010	1,389	1,242

SPENDING CATEGORY:

Discretionary

The Safe and Drug Free Schools and Communities Act (SDFSCA) funds programs in schools, communities, and institutions of higher education to address the increasing use of illegal substances such as alcohol, cigarettes, and drugs among youth and the related issue of violence in schools. Approximately 97 percent of the nation's school districts receive funding under the act, and generally students in grades 5 through 12 participate in the programs. The wide distribution of SDFSCA funding has led to questions about whether such aid might be more effective if it was focused on areas or groups of people with the greatest need.

In fiscal year 2000, states received $445 million of the program's total funding of $565 million. Half of each state's award is based on its school-age population, and half is based on the number of poor children in the state. The law requires states to distribute 80 percent of their grants to school districts, primarily on the basis of enrollment. The remaining 20 percent of state grants go to the governors for services to groups not served by the education system, such as incarcerated youth and school dropouts. Little evidence is available to date about whether SDFSCA programs reduce rates of substance use and violence among youth. However, research shows that the programs have been effective in increasing awareness about the consequences of drug use.

This option would reduce funding to the states by 15 percent and require them to direct the remaining funds toward areas or groups of people considered most likely to benefit from such grants. The option would reduce federal outlays by $5 million in 2001 and $791 million over the 2001-2010 period.

To better target SDFSCA grants, the federal government could change the formula for allocating funds among the states, reduce the number of school districts within states that may receive grants, or target certain age groups within the schools. For instance, federal grant amounts could be tied to a "need" indicator such as state rates of crime or drug use. Similarly, states in their turn could be required to allocate grants to school districts either on the basis of need or through a competitive process. The federal government could also require states to focus funds on children in the earlier grades. That proposal stems from research indicating that prevention programs might be most effective in changing those students' attitudes about drugs and violence.

Focusing SDFSCA funds, as this option provides, could have several different effects. Districts with less crime and fewer drug problems might not receive grants, whereas districts with higher levels of need might receive grants large enough to implement somewhat more comprehensive drug and violence prevention programs than are possible with the current level and distribution of federal funds. Yet even in areas with low rates of crime and drug use, prevention programs may serve a proactive function by raising people's awareness of the problem. If such programs were eliminated, drug use and violence might accelerate and lead to even more costly interventions on the part of school systems and the community.

500-08-A Eliminate Interest Subsidies on Loans to Graduate Students

	Outlay Savings (Millions of dollars)
2001	365
2002	520
2003	520
2004	535
2005	545
2001-2005	2,485
2001-2010	5,340

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

500-08-B and 500-08-C

Federal student loan programs afford students and their parents the opportunity to borrow funds to attend postsecondary schools. Those programs offer three types of loans: "subsidized" loans to students who are defined as having financial need, "unsubsidized" loans to students regardless of need, and loans to parents of students. Two programs provide all three types of loans; they are the Federal Family Education Loan Program, in which loans made by private lenders are guaranteed by the federal government, and the Ford Federal Direct Student Loan Program, in which the government makes the loans through schools. With all of the loans, borrowers benefit because the interest rate charged is lower than the rates most of them could secure from alternative sources. With subsidized loans, borrowers benefit further because the federal government pays the interest on the loans while students are in school and during a six-month grace period after they leave.

Federal costs could be reduced by limiting eligibility for subsidized loans to undergraduate students. Graduate students could substitute unsubsidized loans for the subsidized loans they had received previously. That change would reduce federal outlays by $365 million in 2001 and $5.3 billion over the 2001-2010 period.

Restricting subsidized loans to undergraduate students would direct funds toward achieving the goal of making an undergraduate education affordable. Because graduate students have completed their undergraduate work, they are outside the group of students that constitutes the federal government's particular focus. Under this option, graduate students who took unsubsidized loans to replace the subsidized loans they had lost would ultimately be responsible for somewhat higher loan payments. However, the federal student loan programs have several options for making repayment manageable for students who have high loan balances or difficult financial circumstances.

Nevertheless, graduate students often amass large student loan debts because of the number of years of schooling required for their degrees. Without the benefit of interest forgiveness while they were enrolled in school, their debt would be substantially larger when they entered the repayment period because the interest on the amounts they had borrowed over the years would be added to their loan balance.

500-08-B Increase Origination Fees for Unsubsidized Loans to Students and Parents

	Outlay Savings (Millions of dollars)
2001	100
2002	155
2003	160
2004	160
2005	165
2001-2005	740
2001-2010	1,655

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

500-08-A and 500-08-C

The government recoups part of the cost of insuring student loans by collecting 3 percent of the face value of each loan from students and their parents as an origination fee. (Guaranty agencies may collect an additional 1 percent of the face value as an insurance fee to replenish the federal reserve fund they manage, but since 1998, very few have done so.) The fees are charged on subsidized, unsubsidized, and PLUS loans (Parent Loans to Undergraduate Students).

Under this option, the origination and insurance fees in the Federal Family Education Loan Program (FFELP) would be set to equal the origination fee on the comparable loan in the Ford Federal Direct Student Loan Program. In addition, fees in both programs on unsubsidized and PLUS loans would be 1 percent higher (or 4 percent) than fees on subsidized loans (which are 3 percent). To implement the changes, the Congress would have to require the guaranty agencies to collect the 1 percent insurance fee on all FFELP loans and the Department of Education to collect a 1 percent higher fee on the FFELP's counterpart loan in the direct student loan program. Those changes would reduce program outlays by $100 million in 2001 and $1.7 billion over the 2001-2010 period.

An argument for the change is that even with the higher origination fees, many students would still benefit substantially from the loans, in part because the government guarantees them. The guarantee means that lenders are willing to make loans to students who do not have a credit history and to make them at interest rates below those available on most private loans. Furthermore, during the first five years of repayment, many borrowers can subtract the interest on the loans from their income for the purpose of calculating federal income taxes. And because the change in the origination fees would affect only unsubsidized and PLUS loans, it would produce savings without affecting the value of subsidized loans received by the neediest students.

Increasing the origination fees, however, would reduce the net proceeds from any given loan. As a result, students would need to secure larger loans to finance the same amount of education. That could pose a problem for many students who were already borrowing the maximum allowed by law and would not be able to borrow more.

500-08-C Restrict Eligibility for Subsidized Student Loans by Including Home Equity in the Determination of Financial Need

	Outlay Savings (Millions of dollars)
2001	65
2002	90
2003	90
2004	95
2005	95
2001-2005	435
2001-2010	910

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

500-08-A and 500-08-B

The Higher Education Amendments of 1992 eliminated home equity from consideration in determining how much a student's family is expected to contribute to cover educational expenses—a change that has made it easier for many students to obtain subsidized student loans. The amount a family is expected to contribute is determined by what is essentially a progressive tax formula. In effect, federal calculations "tax" family incomes and assets above the amounts assumed to be required for a basic standard of living. Since 1992, the definition of assets has excluded home equity for all families and excluded all assets for applicants whose income is below $50,000.

Under this option, home equity would be included in calculating a family's need for financial aid for postsecondary education. In addition, the income threshold under which most families are not asked to report their assets would be lowered from $50,000 to its previous level of $15,000. Home equity would be "taxed," as other assets are now, at rates of up to about 5.6 percent after a deduction for allowable assets. The change would result in fewer students qualifying for subsidized loans or more students qualifying for subsidized loans of smaller amounts. Overall, by including home equity, outlays could be reduced by about $65 million in 2001 and $910 million during the 2001-2010 period.

Not counting home equity gives families who own a house an advantage over those who do not. In today's economy, borrowing against home equity at an affordable interest rate is relatively simple. If families were unable or unwilling to take out home equity loans, students could take unsubsidized loans to finance the family's expected contribution. That approach would cause relatively little difficulty for families' budgets because the interest payments on unsubsidized loans can be postponed while the student is in school. The interest is then simply added to the accumulated loan balance when the student leaves school and begins repayment.

However, because increases in incomes have not always kept pace with increases in housing prices, some families might have difficulty repaying their mortgage if they borrowed against home equity to finance their children's education. In addition, having to value their home and other assets would complicate the loan application process for many families.

500-09 Reduce Special Allowance Payments to Lenders in the Student Loan Program

	Outlay Savings (Millions of dollars)
2001	235
2002	385
2003	345
2004	0
2005	0
2001-2005	965
2001-2010	965

SPENDING CATEGORY:

Mandatory

The largest federal student loan program is the Federal Family Education Loan Program, which guarantees 98 percent reimbursement on defaulted loans made by private lenders to eligible students. Under the program, students and the federal government together pay lenders an interest rate each year that is based on changes in a reference rate determined in the financial markets. The federal payments are called special allowance payments; their purpose is to approximate a fair market return to lenders while subsidizing the cost to students of financing their education. One such payment, which was added by the Higher Education Amendments of 1998 and modified in 1999, applies to subsidized and unsubsidized loans made after October 1, 1998, and before July 1, 2003. Under that provision, the federal government will make payments to lenders that CBO estimates will average about 0.35 percentage points between October 1, 2000, and July 1, 2003. This option would eliminate that payment on all new subsidized and unsubsidized loans. Savings would total $235 million in 2001 and $965 million over the 2001-2003 period, at the end of which the provision would expire.

An argument for reducing the special allowance payment is that in most cases, it is not needed for lenders to achieve a fair market rate of return on their loans. By using a reference rate that closely mirrors the interest rate that lenders pay on their own debts, the government has assured lenders a stable net income from such loans. Moreover, nearly the entire loan amount is guaranteed by the federal government. In addition, a 1998 study by the Department of the Treasury concluded that even with a 0.5 percentage-point lower yield on loans made under the program, lenders would earn returns that, on average, would be sufficient to make the business attractive.

The argument for retaining the payment is that without it, some lenders would, indeed, receive unacceptably low rates of return and leave the program. Such pruning of the lender ranks could create difficulties for financial aid officers who administer student financial aid at postsecondary institutions and for students who seek loans. In general, student loans are quite small compared with, for example, mortgage loans, but the costs of servicing them are not proportionately lower. As a result, the interest rate necessary to yield sufficient income to cover the costs of servicing needs to be higher. Furthermore, servicing costs vary by the size of the loan and the characteristics of the student, so reducing the profit margin for lenders might induce them to stop making loans to some students. Another risk of paying lenders less than a fair market rate of return is that they might substantially reduce their investments in improving the quality of loan servicing or stop adapting their package of loan services to the particular needs of the institutions that participate in the loan program.

500-10 Eliminate Administrative Fees Paid to Schools in the Campus-Based Student Aid and Pell Grant Programs

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	164	18
2002	164	159
2003	164	164
2004	164	164
2005	164	164
2001-2005	820	669
2001-2010	1,640	1,489
Relative to WIDI		
2001	167	19
2002	169	161
2003	172	170
2004	175	173
2005	178	176
2001-2005	861	700
2001-2010	1,798	1,624

SPENDING CATEGORY:

Discretionary

In two types of federal student aid programs, the government pays schools to administer the programs or to distribute the funds, or both. In campus-based aid programs, which include Federal Supplemental Educational Opportunity Grants, Federal Perkins loans, and Federal Work-Study Programs, the government distributes funds to institutions that in turn award grants, loans, and jobs to qualified students. Under a statutory formula, institutions may use up to 5 percent of program funds for administrative costs. Similarly, in the Federal Pell Grant Program, the schools distribute the funds, although eligibility is determined solely by federal law. The Higher Education Act provides for a federal payment of $5 per Pell grant to reimburse schools for a share of their costs of administering the program.

The federal government could save about $144 million a year if schools were not allowed to use federal funds from the campus-based aid programs to pay for administrative costs. The government could save another $20 million if the $5 payment to schools in the Pell Grant program was eliminated. Together, those options would produce savings of $18 million in 2001 and $1.5 billion over the 2001-2010 period.

Arguments can be made both for eliminating the administrative payments and for retaining them. On the one hand, institutions benefit significantly from participating in federal student aid programs even without the payments because the aid makes attendance at the schools more affordable. In 2000, students will receive an estimated $10.9 billion in federal funds under the Pell Grant and campus-based aid programs.

On the other hand, the institutions do, indeed, incur costs for administering the programs. Furthermore, if the federal government does not pay those expenses, schools will simply pass along the costs to students in the form of higher tuition or fees.

500-11 Eliminate the Leveraging Educational Assistance Partnership Program

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	40	8
2002	40	41
2003	40	41
2004	40	40
2005	40	40
2001-2005	200	170
2001-2010	400	370
Relative to WIDI		
2001	41	8
2002	41	41
2003	42	41
2004	43	42
2005	43	43
2001-2005	210	175
2001-2010	439	401

SPENDING CATEGORY:

Discretionary

The Leveraging Educational Assistance Partnership (LEAP) program, formerly the State Student Incentive Grant program, helps states provide financially needy postsecondary students with grant and work-study assistance while they attend either academic institutions or schools that teach occupational skills. States must match federal funds at least dollar for dollar and also meet maintenance-of-effort criteria. Unless excluded by state law, all public and private nonprofit postsecondary institutions in a state are eligible to participate in the LEAP program.

Eliminating the program would save $8 million in 2001 and $370 million over the 2001-2010 period. The extent of the actual reduction in student assistance would depend on the responses of states, some of which would probably make up at least part of the lost federal funds.

Proponents of eliminating this program argue that it is no longer needed to encourage states to provide more student aid. When the LEAP program was first authorized in 1972, only 28 states had student grant programs; now, all 50 states provide such grants.

An argument against eliminating the LEAP program is that not all states would increase their student aid appropriations to make up for the lost federal funding and some might even reduce them. In that case, some students who received less aid might not be able to enroll in college or might have to attend a less expensive school.

500-12 End New Funding for Perkins Loans

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	100	10
2002	100	97
2003	100	100
2004	100	100
2005	100	100
2001-2005	500	407
2001-2010	1,000	907
Relative to WIDI		
2001	102	10
2002	103	99
2003	105	103
2004	107	105
2005	109	107
2001-2005	526	425
2001-2010	1,097	988

SPENDING CATEGORY:

Discretionary

The federal government provides student loans through three programs: Federal Family Education Loans, Ford Federal Direct Student Loans, and Federal Perkins Loans (formerly National Defense Student Loans). The Perkins Loan program is the smallest, with allocations made directly to approximately 2,000 postsecondary institutions. Financial aid administrators at those schools then determine which eligible students receive Perkins loans. During the 1999-2000 academic year, approximately 700,000 students will receive such loans.

The money for Perkins loans comes from an institutional revolving fund, totaling approximately $1.1 billion in 2000, that has four sources: collections by the schools of payments on prior year student loans ($945 million in 2000), federal payments for loan cancellations granted in exchange for teaching in high-need areas or for military or public service ($30 million in 2000), federal contributions from new appropriations ($100 million in 2000), and institutional matching contributions that for each school must equal at least one-third of the federal contribution.

Eliminating new appropriations for federal contributions would lower outlays by $907 million during the 2001-2010 period. The extent of the reduction in funds for student loans would depend on the responses of postsecondary institutions, some of which would make up part or all of the lost federal money. If institutions made up none of the lost federal funds but continued to contribute to the program at the level of their previous matching share, approximately 64,000 fewer Perkins loans would be made.

Reflecting the view that the main goal of federal student aid is to provide access to postsecondary education for needy students, the primary justification for this option is that the program may be failing to provide equal access to equally needy students. Federal contributions are allocated, first, on the basis of an institution's 1985 allocation and, second, on the basis of the financial need of its students. Because campus-based aid is tied to specific institutions, students with greater need at poorly funded schools may receive less than those with less need at well-funded institutions.

Eliminating new funds for Perkins loans, however, would reduce the discretion of postsecondary institutions in packaging aid to address the special situations of some students. It would also reduce total available aid. Moreover, Perkins loans disproportionately help students at private nonprofit institutions (whose students get almost half of the aid, compared with about 20 percent of Pell Grant aid). Thus, cutting Perkins loans would make that type of school less accessible to needy students.

500-13 Reduce Funding for the Arts and Humanities

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	120	75
2002	120	110
2003	170	165
2004	170	170
2005	170	170
2001-2005	750	690
2001-2010	1,600	1,540
Relative to WIDI		
2001	145	95
2002	170	150
2003	245	235
2004	275	270
2005	310	300
2001-2005	1,145	1,050
2001-2010	3,160	3,020

SPENDING CATEGORY:

Discretionary

The federal government subsidizes various activities related to the arts and humanities. In 2000, combined funding for several programs totaled just over $1 billion; it included federal appropriations for the Smithsonian Institution ($440 million), the Corporation for Public Broadcasting ($310 million), the National Endowment for the Humanities ($116 million), the National Endowment for the Arts ($98 million), the National Gallery of Art ($68 million), the John F. Kennedy Center for the Performing Arts ($34 million), and the Institute of Museum Services ($24 million).

Cutting funding for those programs by 15 percent would reduce federal outlays over the 2001-2010 period by over $1.5 billion. (Savings from a reduction in funding for the Corporation for Public Broadcasting would not be realized until 2003 because the program receives its appropriations two years in advance.) The actual effect on arts and humanities activities would depend in large part on the extent to which other funding sources—states, localities, individuals, firms, and foundations—increased their contributions.

Some proponents of reducing or eliminating funding for the arts and humanities argue that support of such activities is not an appropriate role for the federal government. Other advocates of cuts suggest that the expenditures are particularly unacceptable when programs addressing central federal concerns are not being funded fully. Some federal grants for the arts and humanities already require nonfederal matching contributions, and over half of all museums charge or suggest that patrons pay an entrance fee. Those practices could be expanded to accommodate a reduction in federal funding.

However, critics of cuts in funding contend that alternative sources would be unlikely to fully offset the drop in federal subsidies. Subsidized projects and organizations in rural or low-income areas might find it especially difficult to garner increased private backing or sponsorship. Thus, a decline in government support, opponents argue, would reduce activities that preserve and advance the nation's culture and that introduce the arts and humanities to people who might not otherwise have access to them.

500-14 Eliminate Funding for the Senior Community Service Employment Program

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	440	80
2002	440	400
2003	440	440
2004	440	440
2005	440	440
2001-2005	2,200	1,800
2001-2010	4,400	4,000
Relative to WIDI		
2001	445	80
2002	455	410
2003	460	455
2004	470	465
2005	480	470
2001-2005	2,310	1,880
2001-2010	4,825	4,360

SPENDING CATEGORY:

Discretionary

The Senior Community Service Employment Program (SCSEP) funds part-time jobs for people age 55 and older who are unemployed and who meet income eligibility guidelines. To be eligible to participate in the program in 1999, an individual's annual income had to be below roughly $10,000, which was 125 percent of the federal poverty guideline for a person living alone. Through SCSEP, which is authorized under title V of the Older Americans Act, grants are awarded to several nonprofit organizations, the U.S. Forest Service, and state agencies. The sponsoring organizations and agencies pay participants to work in part-time community service jobs, up to a maximum of 1,300 hours per year.

SCSEP participants work in schools, hospitals, and senior citizen centers and on beautification and conservation projects. They are paid the higher of the federal or state minimum wage or the local prevailing rate of pay for similar employment. Participants also receive annual physical examinations, training, personal and job-related counseling, and assistance to move into private-sector jobs when they complete their projects.

Eliminating SCSEP would reduce outlays over the 2001-2010 period by about $4 billion. Opponents of the program maintain that it offers few benefits aside from income support and that the presumed value of the work experience gained by SCSEP participants would generally be greater if the experience was provided to equally disadvantaged young people, who have longer careers over which to benefit. In addition, the costs of producing the services now provided by SCSEP participants could be borne by the organizations that benefit from their work; under current law, those organizations bear only 10 percent of such costs. That shift would ensure that only those services that were most highly valued would be provided.

SCSEP, however, is the major federal jobs program aimed at low-income older workers, providing jobs for nearly 100,000 of them in 1998. Eliminating the program could cause hardship for older workers who were unable to find comparable unsubsidized jobs. In general, older workers are less likely than younger workers to be unemployed, but those who are take longer to find work. Moreover, without SCSEP, community services might be reduced if nonprofit organizations and states were unwilling or unable to increase expenditures to offset the loss of federal funds.

500-15 Eliminate Funding for the National and Community Service Act

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	415	40
2002	430	190
2003	430	300
2004	435	370
2005	435	405
2001-2005	2,145	1,305
2001-2010	4,320	3,505
Relative to WIDI		
2001	430	40
2002	455	195
2003	470	315
2004	480	385
2005	490	430
2001-2005	2,325	1,365
2001-2010	4,950	3,820

SPENDING CATEGORY:

Discretionary

As a reward for providing community service, students may receive aid from the federal government to attend postsecondary schools through the National and Community Service Act. The act funds the AmeriCorps Grants Program, the National Civilian Community Corps (NCCC), Learn and Serve America, and the Points of Light Foundation, with AmeriCorps receiving the majority of the total appropriation. Those programs provide assistance for education, public safety, the environment, and health care, among other services. In many cases, the programs build on existing federal, state, and local programs. The AmeriCorps Grants Program and NCCC provide participants with an educational allowance, a stipend for living expenses, and, if they need them, health insurance and child care. Learn and Serve America participants generally do not receive stipends or education awards but may receive academic credit toward their degrees. Much of the total financial resources available for the AmeriCorps Grants Program comes from state and local governments and from private enterprises.

Eliminating federal funding for those programs would save $3.5 billion over the 2001-2010 period. (The estimate includes costs associated with terminating the programs.) Alternatively, some of the savings from eliminating the programs could be redirected to the Federal Pell Grant Program, which is more closely targeted toward low-income students.

Some critics who favor eliminating the programs maintain that community service should be voluntary rather than an activity for which a person is paid. An additional justification for this option is based on the view that the main goal of federal aid to students should be to provide access to postsecondary education for people with low income. Because participation in the programs is not based on family income or assets, funds do not necessarily go to the poorest students.

Supporters of the programs argue, however, that in addition to providing valuable services, the programs enable many students to attend postsecondary schools. Moreover, they believe that opportunities to engage in national service can promote a sense of idealism among young people and should be supported.

500-16 Reduce Funding for Head Start

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	1,247	598
2002	1,698	1,574
2003	1,698	1,667
2004	1,698	1,682
2005	1,698	1,682
2001-2005	8,039	7,203
2001-2010	16,529	15,612
Relative to WIDI		
2001	1,312	629
2002	1,849	1,687
2003	1,941	1,867
2004	2,036	1,975
2005	2,131	2,068
2001-2005	9,270	8,226
2001-2010	21,404	20,021

SPENDING CATEGORY:

Discretionary

Since 1965, Head Start has funded grants to local agencies to provide comprehensive services to foster the development of preschool children from low-income families. The services supported by Head Start address the health, education, and nutrition of the children as well as their social behavior. Funds are awarded to about 1,500 grantees at the discretion of the Secretary of Health and Human Services, using state allocations determined by formula. Grantees must contribute 20 percent of program costs from nonfederal funds unless they obtain a waiver. In 1999, the program served about 835,000 children, approximately 60 percent of whom were 4 years old. The average cost per child in Head Start that year was about $5,400 (compared with $7,200 per pupil spent by public elementary and secondary schools).

Reducing the appropriation for Head Start in 2001 and subsequent years to its level for 1996 would reduce federal costs by about $600 million in 2001 and nearly $16 billion over the 2001-2010 period.

The primary argument for reducing funding for Head Start is that there is little evidence of its long-term effectiveness. The evidence that does exist suggests that Head Start does not improve the prospects of participants over the long run. Although the program produces gains in children's intellectual, emotional, and social development after they have been in the program a year, those gains diminish and disappear as participants move through elementary school. Some model early-childhood education efforts have provided evidence of long-term improvement in the lives of participants, but those projects were much more intensive—and expensive—than Head Start and were initiated several decades ago, when the social environment of the country, especially in urban areas, was different. Furthermore, Head Start enrollment and funding have expanded rapidly during the 1990s, and some people question the ability of the program to effectively absorb the additional funds and students. Concerns have been raised as well about the quality of the program's services, including the limited qualifications of some staff.

The main argument against reducing the appropriation for Head Start is that it appears to modestly lessen the probability that participants will be placed in special education programs and to increase the likelihood that students will be promoted to higher grades. Proponents also argue that Head Start enrolls the most severely disadvantaged children and consequently should be credited with preventing participants from falling even further behind in their cognitive, social, and emotional development before they enter elementary school. An additional argument for not cutting Head Start funding is that the program has taken several steps to improve the quality of services that its grantees provide. For example, 50 percent of the increase in appropriations for 2000 must be used for quality improvement activities. A new data collection system is also being developed to produce longitudinal data on a nationally representative sample of participants.

500-17 Reduce the 50 Percent Floor on the Federal Share of Foster Care and Adoption Assistance Payments

	Savings (Millions of dollars) Budget Authority	Outlays
2001	120	90
2002	130	120
2003	140	130
2004	150	140
2005	160	160
2001-2005	700	640
2001-2010	1,670	1,610

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

500-18

The Foster Care and Adoption Assistance programs provide benefits and services to children who are in need. Foster Care supports eligible low-income children who must reside in foster homes; Adoption Assistance subsidizes families that adopt eligible low-income children with special needs.

The federal government and the states jointly pay for the benefits provided by the two programs. The state and federal shares are based on the federal matching rate for medical assistance programs, which depends on a state's per capita income. Higher-income states pay for a larger share of program benefits than do lower-income states. Currently, the federal share for the Foster Care and Adoption Assistance programs can vary between 50 percent and 83 percent. The federal government now pays a 50 percent share in 10 jurisdictions: Colorado, Connecticut, Delaware, the District of Columbia, Illinois, Maryland, Massachusetts, New Hampshire, New Jersey, and New York.

This option would lower the floor on the federal share of benefits from 50 percent to 45 percent. The Congressional Budget Office estimates that this option would save $90 million in 2001 and about $1.6 billion through 2010. Those amounts assume, however, that states would partially offset their higher costs by reducing benefits.

With the 45 percent floor on the federal share of benefits, a state's contribution would relate more directly to its per capita income. As a result, higher-income states that chose to be relatively generous would pay a larger share of their higher benefits. Nevertheless, seven of the 10 jurisdictions would be paying less than the formula alone would require.

In part, however, higher incomes and benefits in the affected jurisdictions reflect higher costs of living and not simply greater wealth and generosity. To accommodate the drop in funding, the jurisdictions would have to reduce Foster Care and Adoption Assistance benefits, cut spending for other services, or raise taxes. If, as CBO's estimates assume, states chose to compensate for their higher costs by partially reducing benefits, the programs' beneficiaries would be adversely affected.

Under the Unfunded Mandates Reform Act of 1995, reductions in federal funding for certain entitlement grant programs—including Foster Care and Adoption Assistance—are considered mandates on state governments if the states lack authority to amend their programmatic or financial responsibilities to offset the loss of funding. Because some states may not have sufficient flexibility within the Foster Care and Adoption Assistance programs to make such changes, this option could constitute an unfunded federal mandate on those jurisdictions under the law.

500-18 Reduce the Federal Matching Rate for Administrative and Training Costs in the Foster Care and Adoption Assistance Programs

	Savings (Millions of dollars) Budget Authority	Outlays
2001	140	115
2002	155	150
2003	170	165
2004	185	180
2005	200	195
2001-2005	850	805
2001-2010	2,150	2,085

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

500-17

The Foster Care and Adoption Assistance programs provide benefits and services to eligible low-income children and families. The federal government pays 50 percent of most administrative costs for the programs, including those for child placement services, and states and local governments pay the remaining share. However, the costs of certain activities are matched at higher rates to induce local administrators to undertake more of them than they would if costs were matched at the 50 percent rate. For example, the federal government pays 75 percent of the costs of training administrators and participating parents.

Reducing the matching rates to 50 percent for all administrative and training expenses in the Foster Care and Adoption Assistance programs would decrease federal outlays by $115 million in 2001 and by almost $2.1 billion over the 2001-2010 period.

Cutting the higher matching rates to 50 percent would be appropriate if the need for special incentives for activities such as training no longer existed. However, states might respond to this option by reducing their administrative efforts, which could raise program costs and offset some of the federal savings. Specifically, states might make less of an effort to eliminate waste and abuse in payments to providers. Alternatively, this proposal might encourage states to provide less training for administrators and prospective foster and adoptive parents or to reduce the payments and other services that the programs offer.

Under the Unfunded Mandates Reform Act of 1995, reductions in federal funding for certain entitlement grant programs—including Foster Care and Adoption Assistance—are considered mandates on state governments if the states lack authority to amend their programmatic or financial responsibilities to offset the loss of funding. Because some states may not have sufficient flexibility within the Foster Care and Adoption Assistance programs to make such changes, this option could constitute an unfunded federal mandate on those jurisdictions under the law.

550

Health

Budget function 550 includes federal spending for health care services, disease prevention, consumer and occupational safety, health-related research, and similar activities. The largest component of spending is the federal/state Medicaid program, which pays for health services for some low-income women, children, and elderly people as well as people with disabilities. CBO estimates that in 2000, the federal government will spend $115 billion on Medicaid and a total of almost $153 billion on function 550. Discretionary outlays make up only $29 billion of that total. Those outlays have grown annually over the past 10 years.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	16.1	18.2	19.6	20.7	22.2	22.8	23.3	25.1	26.4	30.2	33.7
Outlays											
Discretionary	14.9	16.2	18.0	19.6	20.5	22.0	22.6	23.0	24.9	26.9	29.0
Mandatory	42.9	55.0	71.5	79.8	86.6	93.4	96.8	100.9	106.6	114.1	123.6
Total	57.7	71.2	89.5	99.4	107.1	115.4	119.4	123.8	131.4	141.1	152.6
Memorandum:											
Annual Percentage Change in Discretionary Outlays		8.8	11.1	9.3	4.6	7.2	2.5	1.7	8.2	8.4	7.8

550-01 Reduce Funding for the National Health Service Corps

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	29	9
2002	29	21
2003	29	27
2004	29	29
2005	29	29
2001-2005	145	115
2001-2010	290	260
Relative to WIDI		
2001	31	9
2002	33	24
2003	36	31
2004	38	35
2005	40	37
2001-2005	178	136
2001-2010	414	354

SPENDING CATEGORY:

Discretionary

The National Health Service Corps (NHSC), which is administered by the Health Resources and Services Administration, attempts to increase access to primary care services for people who live in designated Health Professional Shortage Areas. The Corps provides scholarships or loan repayment for health professionals in exchange for the recipients' agreeing to serve in a shortage area for a specified period. In recent years, over 2,400 health professionals have been serving with the NHSC—most of them work in underserved rural areas, but about 40 percent are in urban areas. Over half of the participants are doctors, but a substantial fraction of Corps practitioners are dentists, nurse-practitioners, or physician assistants.

This option would reduce budget authority for the NHSC by 25 percent, producing savings in outlays of $9 million in 2001. Five-year savings would total $115 million; savings over the 2001-2010 period would reach $260 million.

Although some people living in underserved areas receive greater access to health services because of the Corps, critics of the program may question whether it distributes health professionals efficiently. Concerns center on whether the services that an NHSC professional provides in an underserved area outweigh the value of the services that he or she would have provided in some other location by enough to justify the public expense of a scholarship or loan repayment. Moreover, some NHSC participants may displace other health professionals. For example, certain of the more desirable shortage areas might have been able to attract health professionals if a number of the potential patients were not already being served by Corps professionals. In addition, some observers might question whether NHSC funding represents a good return on investment. Although retention rates have increased substantially, almost half of the recruits do not remain in their underserved location beyond their obligation.

Reducing funding for the NHSC would lessen access in some underserved areas to the services provided by health professionals, although the Corps might be able to mitigate the effects of budget cuts by spending more of its resources on relatively inexpensive nonphysician providers. But even if the Corps refocused its remaining funds on nonphysician practitioners, the services of those professionals would not fully substitute for the skills and services offered by physicians. In the event of a cut in funding, community health centers, which obtain about a quarter of their physicians from the NHSC, would probably reduce their services. Moreover, lower levels of funding would probably have a disproportionate impact on people from minority groups, who constitute the majority of patients served by Corps professionals.

550-02 Reduce the Floor on the Federal Matching Rate in Medicaid

	Outlay Savings (Millions of dollars)
2001	3,750
2002	4,060
2003	4,400
2004	4,790
2005	5,220
2001-2005	22,230
2001-2010	56,180

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

550-03

The Medicaid program pays for medical assistance for certain low-income families, for low-income people who receive Supplemental Security Income, and for other low-income individuals—mostly children and pregnant women. The federal government and the states pay for the program jointly, with the federal government's share generally varying according to a formula that depends on a state's per capita income. High-income states pay for a larger share of benefits than low-income states, but by law, the federal share can be no less than 50 percent and no more than 83 percent. In 2001, the 50 percent floor will apply to nine states: Colorado, Connecticut, Delaware, Illinois, Maryland, Massachusetts, New Hampshire, New Jersey, and New York. (The floor would also have applied to the District of Columbia, but the Balanced Budget Act of 1997 established a permanent special exception for that jurisdiction.)

Under this option, the 50 percent floor would be reduced to 45 percent, generating savings of about $3.7 billion in 2001 and $22.2 billion through 2005. (The option assumes that matching rates for other programs that are jointly funded by the federal and state governments would be unaffected, even though some programs have matching rates that are tied to the rate for Medicaid. Savings would be greater if matching rates in those programs also changed.)

Proponents of this change argue that the allocation formula does not adequately address differences in the tax base of the states and that high-income states should bear a larger share of the cost of their programs. If the floor was reduced to 45 percent, federal contributions would be more closely related to the state's per capita income, and six of the nine jurisdictions would still be paying less than the formula alone would require.

Opponents of reducing the 50 percent floor believe that higher incomes in the affected states partly reflect higher costs of living. If the option was adopted, those states would have to compensate for the lower matching rates by either reducing Medicaid benefits, reducing expenditures for other services, or raising taxes.

550-03 Reduce the Enhanced Federal Matching Rates for Certain Administrative Functions in Medicaid

	Outlay Savings (Millions of dollars)
2001	670
2002	810
2003	1,050
2004	1,140
2005	1,240
2001-2005	4,910
2001-2010	12,750

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

550-02, 550-04-A, and 550-04-B

Under current law, the federal government pays part of the costs that states incur in administering their Medicaid programs. For most administrative activities, the federal matching rate is 50 percent, but that rate is higher for certain activities. For example, the federal government pays 75 percent of the costs of skilled medical professionals who are employed in Medicaid administration, 75 percent of the costs of utilization review, 90 percent of the development costs of systems for claims processing and management information, and 75 percent of the costs of operating such systems.

The purpose of enhanced matching rates is to give states incentives to develop and support particular administrative activities that the federal government considers important for the Medicaid program. But once the administrative systems are operational, there may be less reason to continue to pay higher rates. If the federal share of all Medicaid administrative costs was 50 percent, savings would be $670 million in 2001, $4.9 billion over the 2001-2005 period, and $12.8 billion over the 2001-2010 period.

Without high matching rates, states might be inclined to cut back on some activities, with adverse consequences for the quality of care and for program management. States might, for example, hire fewer nurses to conduct utilization review and oversee care in nursing homes, or they might undertake fewer improvements to their management information systems. However, if the Congress wished to protect certain administrative functions, it could maintain the higher matching rates for some administrative activities and reduce them for others.

550-04-A Restrict the Allocation of Common Administrative Costs to Medicaid

	Outlay Savings (Millions of dollars)
2001	290
2002	330
2003	390
2004	390
2005	390
2001-2005	1,790
2001-2010	3,740

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

550-03 and 550-04-B

Public assistance programs have certain administrative requirements that are common to the enrollment process, such as the collection of information on a family's income, assets, and other characteristics. Before the 1996 welfare reform law, the three major public assistance programs—Aid to Families with Dependent Children (AFDC), Food Stamps, and Medicaid—all reimbursed states for 50 percent of most of their administrative costs. But states usually charged the common administrative costs of those programs to AFDC.

The welfare reform law replaced AFDC and some related programs with the Temporary Assistance for Needy Families (TANF) block-grant program. The block grants that states receive are based on historical federal welfare expenditures, including administrative costs. Thus, insofar as states had previously paid for the common administrative costs of public assistance programs out of AFDC funds, those amounts are now included in their block grants. Although the welfare reform act is silent about the cost allocation process, the Department of Health and Human Services now requires states to charge part of the common administrative costs of Medicaid and TANF to Medicaid, even if those costs are already included in the states' TANF block grants.

This option would reduce federal reimbursement for Medicaid administrative costs to reflect the share of those costs that are assumed to be covered by the TANF block grant; it would also prohibit states from using TANF funds to pay for those costs. The amount of the reduction would be about one-third of the common costs of administering the Medicaid, AFDC, and Food Stamp programs that were charged to AFDC during the base period used for determining the amount of the TANF block grant. (A similar adjustment has already been made in the amount the federal government pays the states for the administrative costs of the Food Stamp program.) Savings would be $290 million in 2001, $1.8 billion over the 2001-2005 period, and $3.7 billion over the 2001-2010 period. (If, however, the policy permitted the states to use TANF funds to pay for those costs, savings would be $170 million in 2001, $2 billion over the 2001-2005 period, and $2.4 billion over the 2001-2010 period.)

The reductions would come at a time when states are attempting to expand their outreach activities to enroll more eligible children in Medicaid and the State Children's Health Insurance Program (SCHIP). Because the share of SCHIP spending that can be devoted to administration is capped, states may seek to increase the share of the administrative burden that Medicaid bears. But states would be less likely to pursue that strategy if Medicaid administrative payments were reduced. Reducing those payments might result in fewer eligible people being enrolled in Medicaid.

550-04-B Reduce Spending for Medicaid Administration

	Outlay Savings (Millions of dollars)
2001	1,680
2002	1,810
2003	2,030
2004	2,310
2005	2,620
2001-2005	10,450
2001-2010	29,460

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

550-03 and 550-04-A

An alternative strategy to limit federal payments for Medicaid's common administrative costs would base those payments to the states on matching payments for administrative costs in the period before the Temporary Assistance for Needy Families (TANF) block-grant program was established. Under this option, the federal government would cap the amount per enrollee that it paid the states for Medicaid administration. The per capita limit would grow at 5 percent a year from the base-year amount, which would be the administrative costs per enrollee for which the states claimed matching payments in 1996. Savings would be $1.7 billion in 2001, $10.5 billion over the 2001-2005 period, and $29.5 billion over the 2001-2010 period.

Using this approach, states that before TANF allocated Medicaid's common administrative costs to AFDC would not have those costs included in their projected Medicaid administrative costs. But states that claimed those costs through the Medicaid program would have them built into their Medicaid administrative cost base. The option would generate large savings because the actual average rate of growth of administrative costs was more than 5 percent a year in the 1996-1999 period and is also projected to exceed 5 percent in 2000 and later years.

550-05 Convert Medicaid and Medicare DSH Payments into a Block Grant

	Outlay Savings (Millions of dollars)
2001	1,160
2002	2,160
2003	2,690
2004	2,970
2005	3,340
2001-2005	12,330
2001-2010	33,550

SPENDING CATEGORY:

Mandatory

Under current law, states are required to adjust Medicaid payments to hospitals that treat large numbers of low-income and Medicaid patients, which are known as disproportionate share (DSH) hospitals. In the early 1990s, some states used creative financing mechanisms to generate large federal matching payments through the DSH program, and federal DSH costs soared. To curb that growth, the Congress enacted a series of restrictions on DSH payments, culminating in those in the Balanced Budget Act of 1997. Federal outlays for Medicaid DSH payments were $8.5 billion in 1999 and are projected to decline to $8.1 billion by 2002, when they will start to rise with inflation.

In addition to Medicaid DSH payments, hospitals that serve a disproportionately large share of low-income patients may also receive higher payment rates under Medicare's prospective payment system. Implemented in 1986, the Medicare disproportionate share adjustment was intended to account for the presumably higher costs of treating Medicare patients in such hospitals. Recently, however, the adjustment has been seen more as a means to protect access to care for Medicare and low-income populations by providing financial support to hospitals serving large numbers of indigent patients. Outlays for Medicare DSH payments rose rapidly between 1989 and 1997, reaching $4.5 billion in 1997. Under the Balanced Budget Refinement Act of 1999, a 4 percent reduction in Medicare DSH adjustments is set to expire in 2002. As a result, payments in 2002 will be $5.3 billion.

An alternative approach to providing federal financial support for health care institutions that serve the poor and uninsured would be to convert the current Medicaid and Medicare disproportionate share programs into block grants to the states. The grants could be constrained to grow more slowly than DSH payments would grow under current law. In exchange for slower growth, states could be given flexibility to use the funds to meet the needs of their low-income uninsured populations in the most cost-effective ways.

Under this illustrative option, which assumes a maintenance-of-effort requirement for states, the aggregate block grant in 2001 would be the sum of Medicare DSH payments and Medicaid DSH allotments for 2000, reduced by 10 percent. In subsequent years, the block grant would be indexed to the increase in the consumer price index for urban consumers less 1 percentage point. Additional savings would accrue to Medicare because lower DSH payments would reduce payment updates to plans participating in Medicare+Choice. Total savings would be $1.2 billion in 2001, $12.3 billion for the 2001-2005 period, and $33.6 billion for the 2001-2010 period.

Giving the states more discretion in the allocation of DSH payments could result in those funds being targeted more appropriately and equitably to facilities and providers that serve low-income populations. But allowing the states to allocate the payments could cause some large urban hospitals to receive considerably less public funding than they do now, possibly threatening their future survival. In addition, determining how to allocate the block grant funds among the states would be difficult and controversial.

550-06 Recover Unspent Funds from the State Children's Health Insurance Program

	Outlay Savings (Millions of dollars)
2001	40
2002	350
2003	370
2004	380
2005	350
2001-2005	1,490
2001-2010	1,880

SPENDING CATEGORY:

Mandatory

The State Children's Health Insurance Program (SCHIP) was established by the Balanced Budget Act of 1997 to provide health insurance to low-income, uninsured children. SCHIP gives states enhanced federal matching funds to cover children whose annual family income is too high to qualify them for Medicaid and who do not have private health insurance. Depending on per capita income in a state, the federal government reimburses between 65 percent and 85 percent of the state's total SCHIP spending (compared with reimbursement of between 50 percent and 83 percent of total Medicaid spending). Funds allocated to a state for a given year are available for three years, after which any unspent funds are to be redistributed to states that have used their respective allotments. The first such redistribution of unspent funds from 1998 is scheduled to take place in 2001.

This option would leave the basic SCHIP program intact but eliminate the redistribution of unspent funds. It would save \$8.5 billion in budget authority and \$1.9 billion in federal outlays during the 2001-2010 period. Most of the outlay savings would occur in the first five years because those are the years in which most of the rollover of funds is expected to occur.

Thus far, states have been slow to spend their SCHIP allotments. The Congress appropriated approximately \$4.2 billion annually for the program for fiscal years 1998 through 2001, \$3.1 billion annually for 2002 through 2004, \$4.1 billion for 2005 to 2006, and \$5.0 billion for 2007. In 1998 and 1999 combined, states spent a total of only about \$1 billion in federal SCHIP funds. CBO estimates that under current law, \$1.9 billion in unspent funds from 1998 will be made available in 2001 to states that have spent their 1998 allotments. The states' slow rate of spending could be the result of the effort involved in planning and implementing large new programs, or it could be attributable to other factors such as uncertainty about future funding or a low level of interest among some states in creating large new programs. An independent study of the program's effectiveness is scheduled to be completed at the end of 2001.

Recovering unspent funds from SCHIP would produce budgetary savings for the federal government with little disruption to most states' plans for providing health insurance to low-income, uninsured children. Because states cannot know in advance how much funding will be available and how those funds will be distributed, they probably do not depend on such funding when they plan and implement their children's health insurance programs.

Eliminating the redistribution of unspent SCHIP funds could, however, reduce the financing flexibility of states that would otherwise use those funds to provide health insurance to low-income children. As a result, those states might not be as ambitious in creating and maintaining their programs as they would be under current law or might spend more money in Medicaid to cover children. Moreover, eliminating the redistribution could take away a potentially useful spending cushion for states that use all of their allotments under the program. That factor could be particularly significant in 2002 through 2004, when overall federal appropriations for SCHIP are slated to decrease by 25 percent.

550-07 Reduce Subsidies for Health Professions Education

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	212	65
2002	212	155
2003	212	195
2004	212	205
2005	212	205
2001-2005	1,060	825
2001-2010	2,120	1,860
Relative to WIDI		
2001	215	65
2002	220	160
2003	225	200
2004	225	220
2005	230	225
2001-2005	1,115	865
2001-2010	2,335	2,040

SPENDING CATEGORY:

Discretionary

The Congress provided $212 million to the Public Health Service in 2000 to fund subsidies to institutions for educating physicians, nurses, and public health professionals. Those funds primarily furnish support through grants and contracts to schools and hospitals for designated training programs in the health professions. The programs promote primary care and community-based training for physicians and other health professionals as well as nursing education:

- o *Primary care and community-based training*. Several programs provide federal grants to medical schools, teaching hospitals, and other training centers to develop, expand, or improve graduate medical education in primary care specialties and other allied health fields and to encourage practice in rural and low-income urban areas. Funding for 2000 is $146 million.

- o *Nursing education*. The subsidies to nursing schools are meant to promote nursing education, including graduate training for nurse administrators, educators, and nursing specialists such as nurse-midwives and nurse-practitioners. Funding for 2000 is $66 million.

Eliminating those grants and subsidies would save about $800 million over the 2001-2005 period. Savings over the 2001-2010 period would be $1.9 billion.

The principal justification for this option is that market forces provide strong incentives for people to seek training and jobs in the health professions. Over the past several decades, the number of physicians—the principal health profession targeted by the subsidies—has rapidly increased, rising from 142 physicians in all fields for every 100,000 people in 1960 to 278 in 1996. In the case of nurses, if a shortage, indeed, existed, higher wages and better working conditions would attract more people to the profession and more trained nurses to nursing jobs, and would encourage more of them to seek advanced training.

The major disadvantage of eliminating the subsidies is that the incentives supplied by market forces may not be strong enough to entirely meet the goals of the health professions programs. For example, third-party reimbursement rates for primary care may not encourage enough physicians to enter those specialties and may not include sufficient financial inducements to increase access to care in rural and inner-city areas. In addition, fewer people might choose advanced training in nursing, which could limit the opportunities for the use of relatively inexpensive physician substitutes.

550-08 Combine and Reduce Public Health Service Block Grants

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	400	145
2002	400	350
2003	400	375
2004	400	390
2005	400	395
2001-2005	2,005	1,655
2001-2010	4,010	3,630
Relative to WIDI		
2001	475	170
2002	540	435
2003	620	530
2004	695	620
2005	770	700
2001-2005	3,095	2,455
2001-2010	8,125	7,090

SPENDING CATEGORY:

Discretionary

In its appropriations for 2000, the Congress provided about $4.0 billion for nine block-grant programs administered by the Health Resources and Services Administration (HRSA), the Centers for Disease Control and Prevention (CDC), and the Substance Abuse and Mental Health Services Administration (SAMHSA).

Four of the nine programs—the Maternal and Child Health Care Block Grant, HIV Care Grants to States, the Family Planning Block Grant, and the Healthy Start Initiative—are administered by HRSA. Those grants support programs that provide child health services, including immunizations, well-child examinations, and services for children with special health care needs; medical care and social support services for people who have been diagnosed with the human immunodeficiency virus; family planning services; and infant mortality efforts. CDC administers the Preventive Health and Health Services Block Grant, which is distributed to the states for programs that support Healthy People 2010, the nation's objectives for promoting health and preventing disease.

The remaining four block grants—the Substance Abuse Performance Partnership Block Grant, the Mental Health Performance Partnership Block Grant, the Projects for Assistance in Transition from Homelessness (PATH) program, and the Protection and Advocacy Program—are administered by SAMHSA. The grants fund substance abuse prevention programs, community-based mental health services for adults with serious mental illnesses and children with severe emotional disturbances, services for people with mental illness or substance abuse disorders who are also either homeless or at risk of becoming homeless, and programs that investigate allegations of abuse and neglect in facilities that provide care for people with mental illness.

This option would combine these funds into two large grants and reduce funding to 90 percent of the 2000 level. The block grants currently administered by HRSA and the CDC would be combined and administered by HRSA, and the block grants currently administered by SAMHSA would be combined and administered by that agency.

The principal justification for this option is that each state would be given added flexibility to direct the grant funds toward programs that the state considers likely to have the most favorable impact. Conditions vary substantially by state, yet grant requirements often compel states to invest resources in programs that may or may not meet a given state's needs. By reducing funds for lower-priority programs, states could allocate additional resources to programs that they considered more important.

The option's major disadvantage is that improved flexibility might not entirely make up for the 10 percent cut in federal funds for state programs. The states would have to make difficult decisions to trim programs that benefited vulnerable population groups. Alternatively, if reducing resources was not feasible, they might have to raise state taxes or cut other state programs.

550-09 Adopt a Voucher Plan for the FEHB Program

	Savings[a] (Millions of dollars)	
	Discretionary[b]	Mandatory
2001	0	0
2002	260	240
2003	520	480
2004	800	740
2005	1,100	1,040
2001-2005	2,680	2,500
2001-2010	13,730	13,140

a. Estimates do not include any savings realized by the U.S. Postal Service.

b. Savings measured from the 2000 funding level adjusted for premium increases and changes in employment.

SPENDING CATEGORIES:

Discretionary and mandatory

RELATED OPTION:

550-10

RELATED CBO PUBLICATION:

Comparing Federal Employee Benefits with Those in the Private Sector (Memorandum), August 1998.

The Federal Employees Health Benefits (FEHB) program provides health insurance coverage for over 4 million active federal employees and annuitants, as well as for their 4.6 million dependents and survivors, at a cost to the government of more than $13 billion in 2000. The cost-sharing structure of the FEHB program encourages federal employees to switch from high-cost to lower-cost plans to blunt the effects of rising premiums; cost sharing also intensifies competitive pressures on all participating plans to hold down premiums. The Balanced Budget Act of 1997 set the federal government's share of premiums for employees and annuitants (including family coverage) at 72 percent of the average weighted premium of all plans beginning January 1, 1999. (The employer's costs are higher under the U.S. Postal Service's collective bargaining agreement.) The act still requires policyholders to pay at least 25 percent of the premium of any particular plan.

To reduce expenditures, the government could offer a flat voucher for health insurance premiums. It could pay the first $2,100 of premiums for employees and retirees ($4,800 for family coverage). Those amounts are based on the government's average expected contribution for nonpostal employees in 2001 and would increase annually by the rate of inflation rather than by the average weighted rate of change for premiums in the FEHB program. Budgetary savings would come from indexing the premiums to inflation rather than to the growth of premiums, which the Congressional Budget Office expects will rise at a rate more than twice that of inflation. Savings in discretionary spending from lower payments for current employees and their dependents would be zero in 2001, $2.7 billion over five years, and $13.7 billion over 10 years. Savings in mandatory spending from reduced payments for retirees would be zero in 2001, $2.5 billion over five years, and $13.1 billion over 10 years.

The option would strengthen price competition among health plans in the FEHB program because almost all current enrollees would be faced with paying all of the incremental premiums above the voucher amount. In addition, removing the requirement that enrollees pay at least 25 percent of the premiums should increase price competition among low-cost plans to attract participants. In the lowest-cost plans, the government would pay almost the entire premium.

On the downside, participants would pay an ever-increasing share of their premiums—possibly over 40 percent by 2005—if premiums rose as expected. The added cost to enrollees could exceed $700 per worker in 2005 and more in later years. Currently, large private-sector plans provide better health benefits for their employees—although not for their retirees—which might make it harder for the government to attract and retain high-quality workers. In addition, for current retirees and long-time federal workers, the option would cut benefits that have already been earned. Moreover, the option could strengthen existing incentives for adverse selection in FEHB plans.

550-10 Base Retiree Health Benefits on Length of Service

	Savings[a] (Millions of dollars) Budget Authority	Outlays
2001	60	60
2002	120	120
2003	180	180
2004	240	240
2005	310	310
2001-2005	910	910
2001-2010	3,830	3,830

a. Estimates do not include any savings realized by the U.S. Postal Service.

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

550-09

RELATED CBO PUBLICATION:

Comparing Federal Employee Benefits with Those in the Private Sector (Memorandum), August 1998.

Federal retirees are generally eligible to continue receiving benefits from the Federal Employees Health Benefits (FEHB) program if they have been participants during their last five years of service and are eligible to receive an immediate annuity. About 80 percent of eligible new retirees elect to receive retiree health benefits. After age 65, FEHB program benefits are coordinated with Medicare; the program pays amounts not covered by Medicare (but no more than the amount it would have paid in the absence of Medicare). Participants and the government share the cost of premiums. The government's share for annuitants and employees is 72 percent of the weighted average premium of all participating plans (up to a cap of 75 percent of the total premium). In 1999, the government paid $4.5 billion in premiums for 1.8 million annuitants and their dependents and survivors.

Under this option, federal retiree health benefits would be reduced for those with relatively short federal careers while preserving the right of retirees to participate in the FEHB program. For new retirees only, the government's share of the premium could be cut by 2 percentage points for every year of service under 30. For example, the government's contribution would fall to 52 percent of the average premium for a retiree with 20 years of service. In 1998, about 55 percent of the roughly 60,000 new retirees who continued in the FEHB program had less than 30 years of service. The average new nonpostal retiree affected by the proposal would pay 48 percent of the premium rather than 28 percent, an annual increase of $830 in 2001. The estimated savings to the government in mandatory spending would total $60 million in 2001 and $910 million over five years. Ten-year savings would rise to $3.8 billion.

The option might make the government's compensation mix fairer and more efficient by improving the link between service and deferred compensation. The option would also help bring federal benefits closer to those available from private firms. Federal retiree health benefits are significantly more generous than those offered by most large private firms, which have been aggressively paring and, in some cases, eliminating retiree health benefits in recent years. A survey of all U.S. employers found that fewer than half provide medical benefits to retirees. And even with this change, federal retiree health benefits would remain comparable with those offered by firms that continued to provide retiree benefits.

A negative aspect of the option is that it would mean a substantial cut in benefits whose effects would be felt most strongly by the roughly 20 percent of new retirees with less than 20 years of service. The option could also encourage some employees with short service careers to delay retirement, whereas others might accelerate retirement plans to avoid the new rules.

550-11 Establish New User Fees for Medical Devices Regulated by the FDA

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	27	20
2002	46	40
2003	38	39
2004	39	39
2005	40	40
2001-2005	190	177
2001-2010	410	393
Relative to WIDI		
2001	27	20
2002	46	40
2003	38	39
2004	39	39
2005	40	40
2001-2005	190	177
2001-2010	410	393

SPENDING CATEGORY:

Discretionary

The Prescription Drug User Fee Act of 1992 (PDUFA) authorized the Food and Drug Administration (FDA) to collect fees from pharmaceutical manufacturers to help speed up the review of applications for marketing and approval of new drugs. The Food and Drug Administration Modernization Act of 1997 reauthorized the PDUFA user fee program but did not address user fees for medical devices. The Congress considered but did not pass legislation authorizing user fees for medical devices in 1994. The Administration's 2001 budget included a proposal to impose user fees on medical devices as well as on other products regulated by the FDA.

Manufacturers must notify the FDA before they market any new medical device, and for certain products, they must obtain approval before marketing them. Imposing fees of $7,000 for each new medical device requiring premarket notification, $3,500 for those devices qualifying for abbreviated or special notification processes, $60,000 for each new medical device needing premarket approval, and $7,000 for each application for a supplemental premarket approval would raise $20 million in 2001 and $393 million during the 2001-2010 period. Taken together, those fees would ultimately constitute about 30 percent of the cost of regulating medical devices. The estimates assume that only a few exemptions would be granted for small businesses or devices with very small markets.

Establishing new user fees for medical devices would require new authorizing legislation. To generate budgetary savings, that legislation would have to permit user fee collections to offset other FDA appropriations for salaries and expenses. PDUFA does not permit that offset for prescription drug user fees.

Proponents of user fees for medical devices argue that regulatory activities benefit both consumers and industry. The FDA's primary function is to ensure public safety by monitoring the quality of pharmaceutical products, medical devices, and food. Firms benefit from the public confidence that results from the FDA's regulation, those proponents maintain, and should therefore bear a share of the costs of those activities.

People who oppose levying new user fees on medical devices might argue that the agency's current oversight of medical devices is excessive and unnecessary. Rather than adding user fees, those opponents might contend that the FDA could cut costs by scaling back its regulatory requirements.

570

Medicare

Budget function 570 comprises spending for Medicare, the federal health insurance program for elderly and eligible disabled people. Medicare consists of two parts, each tied to a trust fund. Hospital Insurance (Part A) reimburses providers for inpatient care that beneficiaries receive in hospitals, as well as care at skilled nursing facilities, home health care related to a hospital stay, and hospice services. Supplementary Medical Insurance (Part B) pays for physicians' services, outpatient services at hospitals, home health care, and other services. CBO estimates that Medicare outlays (net of premiums paid by beneficiaries) will total $199.2 billion in 2000, including discretionary outlays of $3.1 billion.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	2.4	2.6	2.9	2.8	3.0	3.0	2.9	2.6	2.7	2.8	3.1
Outlays											
Discretionary	2.3	2.4	2.8	2.7	2.9	3.0	3.0	2.6	2.6	2.8	3.1
Mandatory	95.8	102.0	116.2	127.9	141.8	156.9	171.3	187.4	190.2	187.7	196.1
Total	98.1	104.5	119.0	130.6	144.7	159.9	174.2	190.0	192.8	190.4	199.2
Memorandum:											
Annual Percentage Change in Discretionary Outlays		6.3	16.4	-6.9	10.0	2.0	-0.6	-12.8	0.5	6.3	12.1

570-01 Reduce Medicare's Payments for the Indirect Costs of Patient Care That Are Related to Hospitals' Teaching Programs

	Outlay Savings (Millions of dollars)
2001	1,300
2002	1,000
2003	1,000
2004	1,100
2005	1,300
2001-2005	5,800
2001-2010	14,100

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-02, 570-03, and 570-04

RELATED CBO PUBLICATION:

Medicare and Graduate Medical Education (Study), September 1995.

The Social Security Amendments of 1983 established the prospective payment system (PPS) under which Medicare pays hospitals for inpatient services provided to beneficiaries. Higher rates are paid to hospitals with teaching programs to cover their higher costs of caring for Medicare patients. Under the Balanced Budget Refinement Act of 1999, the additional percentage paid to teaching hospitals in 2000 will be approximately 6.5 percent for each 0.1 increase in a hospital's ratio of full-time interns and residents to its number of beds. Teaching hospitals will receive 6.25 percent more in 2001 and 5.5 percent more in 2002 and subsequent years for every 0.1 increase in the resident-to-bed-ratio. (Under the Balanced Budget Act of 1997, teaching hospitals would have received 6.0 percent more in 2000 and 5.5 percent more in 2001 and subsequent years for each 0.1 increase in the ratio.)

The Congress enacted the additional payments to teaching hospitals to compensate them for indirect teaching costs—such as the greater number of tests and procedures thought to be prescribed by interns and residents—and to cover higher costs from factors that are not otherwise accounted for in setting the PPS rates. Such factors might include more severely ill patients, a hospital's location in the inner city, and a more costly mix of staffing and facilities, all of which are associated with large teaching programs. (An alternative approach would base additional payments to teaching hospitals on the enhanced value of care in those settings. Such a proposal was recently made by the Medicare Payment Advisory Commission.)

The Prospective Payment Assessment Commission has estimated that a 4.1 percent adjustment to Medicare's payments would more closely match the increase in operating costs associated with teaching. If the teaching adjustment was lowered accordingly, outlays would fall by about $5.8 billion from current-law spending over the 2001-2005 period and by about $14.1 billion over the 2001-2010 period.

This option would better align payments with the actual costs incurred by teaching institutions. Furthermore, since the training that medical residents receive will result in a significant increase in their future income and since hospitals benefit from using residents' labor, it is reasonable for some or all of a hospital's indirect training costs to be borne by both residents and the hospital. Some of those costs are now passed on in the form of stipends that are lower than the value of the residents' services to the hospital. A lower teaching adjustment would probably lead to even lower stipends, however, as well as smaller residency programs. An additional consideration is that if the teaching hospitals now use some payments to fund such activities as charity care, people without health insurance could have less access to health services under this option.

570-02 Reduce Medicare's Direct Payments for Medical Education

	Outlay Savings (Millions of dollars)
2001	800
2002	900
2003	900
2004	1,000
2005	1,000
2001-2005	4,600
2001-2010	10,300

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-01, 570-03, and 570-04

RELATED CBO PUBLICATION:

Medicare and Graduate Medical Education (Study), September 1995.

Medicare's prospective payment system does not include payments to hospitals for the direct costs they incur in providing graduate medical education (GME)—namely, residents' salaries and fringe benefits, teaching costs, and institutional overhead. Instead, Medicare makes those payments separately on the basis of its share of a hospital's 1984 cost per resident indexed for increases in the level of consumer prices. Medicare's direct GME payments, which are received by about one-fifth of all U.S. hospitals, totaled about $2.2 billion for 1999. Under the proposed option, hospitals' direct GME payments would be based on the national average of salaries paid to residents in 1987, updated annually by the consumer price index for all urban consumers. Reimbursement would be based on 120 percent of the national average salary.

In effect, this option would reduce teaching and overhead payments for residents but continue to pay their salaries and fringe benefits. Unlike the current system, under which GME payments vary considerably from hospital to hospital, this option would pay every hospital the same amount for the same type of resident. (Although the Congress took action in 1999 to lessen some of the variation among hospitals in payments per resident, considerable differences remain under current law.) The option would also continue the current-law practice of reducing payments for residents who have gone beyond their initial residency period. The savings from current-law spending would total about $4.6 billion over the 2001-2005 period and about $10.3 billion over the 2001-2010 period.

The overall reduction in the level of subsidies might be warranted since market incentives appear to be sufficient to encourage a continuing flow of new physicians. Moreover, since hospitals use resident physicians to care for patients and since residency training helps young physicians earn higher incomes in the future, both hospitals and residents might reasonably contribute more to those training costs. Residents would contribute more to those costs if hospitals responded to the changes in reimbursements by cutting residents' salaries or fringe benefits.

If hospitals lowered residents' salaries or benefits, the costs of longer residencies—in terms of forgone practice income—could exert greater influence on the young physicians' decisions about pursuing a specialty. More residents might choose to begin primary care practice rather than specialize further. That outcome could be negative for the individual resident; by contrast, the Council on Graduate Medical Education and other groups believe that a relative increase in the number of primary care practitioners would be desirable. Finally, decreasing GME reimbursement could force some hospitals to reduce the resources they commit to training, possibly jeopardizing the quality of their medical education programs.

570-03 Eliminate Additional Capital-Related Payments for Hospitals with Residency Programs

	Outlay Savings (Millions of dollars)
2001	300
2002	300
2003	300
2004	300
2005	400
2001-2005	1,600
2001-2010	3,600

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-01, 570-02, and 570-04

Under the prospective payment system for inpatient hospital services, Medicare pays hospitals an amount for each discharge that is intended to compensate the hospital for capital-related costs. Currently, teaching hospitals receive additional capital-related payments that are based on teaching intensity, measured as a hospital's ratio of residents to its average daily number of inpatients. Specifically, an increase of 0.1 in that ratio raises the hospital's capital-related payment by 2.8 percent.

Eliminating those extra payments would save the Medicare program about $0.3 billion in 2001. Five-year savings would equal about $1.6 billion, and savings over the 2001-2010 period would be $3.6 billion.

In contrast to higher operating costs, which analyses indicate are indeed associated with teaching intensity, a hospital's capital costs per case appear to be unrelated to intensity. Furthermore, paying teaching hospitals more than nonteaching hospitals for otherwise similar patients may discourage efficient decisionmaking by hospitals. In addition, Medicare's payment adjustments for teaching intensity may distort the market for residency training by artificially increasing the value (or decreasing the cost) of residents to hospitals. If residents' training raises the costs of patient care for a hospital, arguably the hospital should bear those costs in order to encourage an efficient amount of training. Hospitals are likely to shift such costs to residents in the form of lower stipends or greater workloads. Residents will engage in such training if they perceive that their future productivity, as reflected in their future incomes, will be great enough to outweigh those costs.

Eliminating the special capital-related payments would reduce revenues to teaching hospitals at a time when those hospitals already face pressures to reduce costs to remain competitive in the growing managed care environment. Teaching hospitals would probably have to reduce some services in response to the decline in their revenues. Those reductions in services could include less provision of public goods, such as research or providing medical care to the indigent.

570-04 Convert Medicare Payments for Graduate Medical Education to a Block Grant and Slow Their Rate of Growth

	Outlay Savings (Millions of dollars)
2001	200
2002	100
2003	200
2004	300
2005	400
2001-2005	1,100
2001-2010	6,000

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-01, 570-02, and 570-03

RELATED CBO PUBLICATION:

Medicare and Graduate Medical Education (Study), September 1995.

Three types of Medicare graduate medical education (GME) payments are tied to the size or intensity of a teaching hospital's residency program: direct graduate medical education payments, the indirect medical education adjustment for inpatient operating costs, and the indirect medical education adjustment for inpatient capital-related costs. Under provisions in the Balanced Budget Act of 1997, teaching hospitals have begun to receive GME payments for participants in Medicare+Choice health plans in addition to the payments that they have traditionally received for fee-for-service Medicare patients. Several variables determine the total amount of GME payments that a hospital receives, including the number and diagnoses of Medicare discharges and numerical factors used for annually updating payments for inpatient operating costs and capital-related costs. Because of changes in those variables over time, the Congressional Budget Office expects GME payments under current law to grow at an average annual rate of 4.3 percent between 2001 and 2010.

This option would replace the current system with a consolidated block grant to fund the special activities of teaching hospitals. Under the current system, a hospital receives GME payments based on regulatory formulas, and total Medicare GME spending is the resulting sum of what Medicare owes each hospital. The option considered here assumes that a switch to the block-grant program would occur in 2001 and that the amount of the grant would be based on spending in 2000, increased for overall inflation. Compared with projected spending under current law, federal outlays would be reduced by $1.1 billion over the first five years and $6.0 billion over the 2001-2010 period.

Establishing a block grant for the three types of GME payments would allow the Congress to better monitor and adjust that funding. Another feature of the option is that Medicare would no longer pay different rates to hospitals for inpatient services merely because of differences in the size or presence of residency programs.

However, because this option would reduce total payments to teaching hospitals below the amounts expected under current law, such hospitals would, on average, receive less revenue than they would otherwise. In response, teaching hospitals might reduce the amount or quality of some of their services or their provision of some public goods, such as medical research or care for indigent people.

570-05 Eliminate Medicare's Additional Payments to Sole Community Hospitals

	Outlay Savings (Millions of dollars)
2001	100
2002	100
2003	100
2004	100
2005	100
2001-2005	500
2001-2010	1,300

SPENDING CATEGORY:

Mandatory

Under Medicare's prospective payment system (PPS) for inpatient hospital services, special rules apply to providers designated as sole community hospitals (SCHs). There are more than 700 SCHs, almost all of which are located in rural areas. Thus, about one-third of rural hospitals qualify for SCH status. Under the current rules, a hospital may be designated as an SCH if it meets specific criteria that define a sole provider of inpatient, acute care hospital services in a geographic area. In addition, some SCHs have been permitted to retain that status regardless of whether they meet the current sole-provider criteria.

Payments to SCHs are generally equal to the highest of three amounts: the regular federal PPS payment that would otherwise apply, an amount based on the hospital's costs in 1982 updated to the current year, or an amount based on the hospital's costs in 1987 updated to the current year. In addition, the Balanced Budget Refinement Act of 1999 allows certain SCHs to be paid according to their fiscal year 1996 costs. Hospitals that choose to receive the regular PPS payment—about half of all SCHs—are eligible to receive higher payment adjustments for disproportionate share status than are other rural hospitals. Hospitals that receive payments based on their updated costs are ineligible for those higher adjustments.

If all sole community hospitals received the regular PPS payment rather than their updated costs, total PPS payments would be about $100 million less in 2001 and $1.3 billion less for the 2001-2010 period. Those savings assume that SCHs would continue to be eligible for higher disproportionate share adjustments.

A primary objective of the SCH rules is to assist hospitals in locations where closings would threaten access to hospital care, but the federal support is not particularly well aimed at such essential providers. Moreover, whether an SCH actually receives higher payments under the special rules that permit payments to be based on a hospital-specific amount depends on whether its costs in any of the specified base years (1982, 1987, or 1996) were relatively high, not on its current financial condition.

If the special payment rules were eliminated, however, revenues of many sole community hospitals would be lower, which might cause financial distress for some of them. And because many SCHs are the sole providers of hospital services in their geographic areas, access to health care or the quality of care might be reduced in some rural locations.

570-06 Institute a Single Global Payment for Hospitals' and Physicians' Services Provided During an Inpatient Stay

	Outlay Savings (Millions of dollars)
2001	100
2002	100
2003	100
2004	100
2005	100
2001-2005	500
2001-2010	1,200

SPENDING CATEGORY:

Mandatory

Hospitals receive payments under Medicare's prospective payment system (PPS) for the operating costs of providing inpatient services to the program's beneficiaries. The payments are determined on a per-case basis; payment rates vary with the patient's diagnosis, which Medicare classifies within a system of diagnosis-related groups (DRGs), and the characteristics of the hospital. Those rates take into account reasonable variations in the treatment of patients with a given DRG and offer an incentive to the hospital to reduce the cost of treatment. PPS payments do not cover all services rendered to patients during the hospital stay. In particular, Medicare pays separately for physicians' services provided on an inpatient basis.

The Health Care Financing Administration (HCFA) has explored the feasibility of making a single global payment for high-cost, high-volume inpatient procedures. That payment would be lower than the separate payments that are now made for hospitals' operating costs and physicians' services. In a recent demonstration project involving heart bypass surgery, discounted payment rates were established through negotiations with participating hospitals in conjunction with teams of physicians. With a global payment, hospitals and physicians alike have an incentive to reduce operating costs while maintaining a satisfactory standard of care. The institutions hoped to offset the discounts in their Medicare payments by two means: improvements in efficiency (and their resultant cost savings) and increases (using new marketing efforts) in the volume of heart bypass patients. During the five-year project, Medicare outlays to the seven hospitals participating in the demonstration averaged about 10 percent less than would have been spent otherwise.

HCFA has also investigated ways to extend the global payment concept. One approach, similar to the heart bypass demonstration, identified other high-cost, high-volume inpatient procedures that might yield negotiated savings. (They included cataract surgery, coronary angioplasty, heart valve replacement, and joint replacement surgery.) That option might be attractive to hospitals, which could market themselves as "centers of excellence." However, such terminology would be controversial because it might be construed as suggesting that other hospitals did not offer high-quality care. Another disadvantage would be that only a modest number of institutions and high-cost procedures might become eligible for global payments. Expanding the use of global payments would yield savings of $100 million in 2001 and $1.2 billion for the 2001-2010 period.

570-07 Increase and Extend the Reductions in the Medicare PPS Market Basket

	Outlay Savings (Millions of dollars)
2001	400
2002	1,000
2003	2,500
2004	4,100
2005	5,900
2001-2005	13,900
2001-2010	75,800

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

570-08

Under Medicare's prospective payment system (PPS), payments for hospitals' operating costs for inpatient services provided to beneficiaries are determined on a per-case basis, according to preset rates that vary with the patient's diagnosis and the characteristics of the hospital. Payment rates are adjusted each year using an update factor that is determined, in part, by the projected increase in the hospital market-basket index (MBI), which reflects increases in hospital costs.

The Balanced Budget Act of 1997 reduced hospital update factors for 1998 through 2002. Specifically, the act froze the basic payment in 1998 and reduced the update by 1.9 percentage points in 1999, 1.8 percentage points in 2000, and 1.1 percentage points in 2001 and 2002. Without those reductions, the updates would have been 2.1 percent in 1998, 2.4 percent in 1999, 2.9 percent in 2000, and more than 3 percent each year in 2001 and 2002. (In several states, however, certain hospitals with negative PPS margins received a 0.5 percentage-point adjustment in 1998 and a 0.3 percentage-point adjustment in 1999.) After 2002, the update factor reverts to the full value of the MBI. If the factor was reduced to the MBI minus 1.8 percentage points in 2001 and stayed at that level throughout the 2001-2010 period, total savings during that time would be $75.8 billion.

In 1997, average profit margins for hospitals on Medicare inpatient services were about 17 percent. Moreover—although the data are not yet complete—MedPAC (the Medicare Payment Advisory Commission) estimates that despite the payment freeze in 1998 and the large reduction in the update factor for 1999, average Medicare inpatient profit margins exceeded 15 percent in both years. Thus, further reductions in update factors could be justified. The American Hospital Association, however, maintains that high inpatient margins reflect major efforts by hospitals to cut costs, which cannot continue indefinitely. Moreover, almost one-quarter of all hospitals have negative profit margins on Medicare inpatient services, so further reductions in payment update factors could cause considerable hardship for those facilities, especially as some hospitals are only now beginning to feel the effects of past payment reductions.

570-08 Reduce Medicare's Payments for Hospitals' Inpatient Capital-Related Costs

	Outlay Savings (Millions of dollars)
2001	300
2002	300
2003	400
2004	500
2005	500
2001-2005	2,000
2001-2010	4,600

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

570-07

In 1992, Medicare revised its method of paying hospitals for their inpatient capital-related costs by replacing cost-based reimbursement with a prospective payment method. Under the prospective system, hospitals receive a predetermined amount for each Medicare patient to pay for capital-related costs, which include depreciation, interest, taxes, insurance, and similar expenses for buildings and fixed and movable equipment. The prospective system applies to about 5,000 hospitals paid under Medicare's prospective payment system for operating costs.

A fully prospective federal payment rate for capital costs is being phased in over 10 years. During the transition period, payments are determined by a complicated method based on a number of factors, including federal and hospital-specific payment rates. The federal and hospital-specific rates are increased annually. By 2001, all hospitals will receive the federal rate, adjusted for the hospital's mix of patients and certain other characteristics.

Analyses conducted by the Health Care Financing Administration (HCFA) suggest that the initial federal and hospital-specific rates were too high. The 1992 rates were based on actual 1989 and 1990 data (for the federal rate and hospital-specific rates, respectively) projected to 1992, but more recent data indicate that the rate of growth of capital costs between 1989 and 1992 was slower than expected. Moreover, the initial level of capital costs per case in 1989 was probably higher than would be optimal in an efficient market because of incentives provided by the Medicare payments. Factors such as changes in capital prices, the mix of patients treated by hospitals, and the "intensity" of hospital services contributed to the overestimate. On the basis of HCFA's analysis, the estimated 1992 capital costs would have been reduced by about 22 percent if those factors had been taken into account.

The federal rate was reduced by 7.4 percent in the Omnibus Budget Reconciliation Act of 1993 in a provision that expired in 1996. The Balanced Budget Act of 1997 reduced the federal rate by 17.8 percent for capital payments made to hospitals for patient discharges occurring in 1998 through 2002. A small part of that reduction, 2.1 percent, will be restored beginning in 2003. A further reduction of 5 percent (bringing the total reduction in capital payments to about the level estimated by HCFA) would yield savings of $300 million in 2001 and $4.6 billion for the 2001-2010 period.

Most hospitals would probably be able to adjust to the reductions by lowering their capital costs or partially covering them with other sources of revenue, because Medicare's payments for capital costs are a small share of hospitals' revenues—less than 5 percent of their total revenues from all sources. Hospitals that are in poor financial condition, however, might have difficulty absorbing the reductions. As a result, the quality of the care they offer might decline, and they might provide fewer services to people without insurance.

570-09 Eliminate Medicare's Payments to Hospitals for Enrollees' Bad Debts

	Outlay Savings (Millions of dollars)
2001	500
2002	600
2003	600
2004	700
2005	700
2001-2005	3,100
2001-2010	7,400

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

570-10

Medicare beneficiaries are responsible for certain deductible and coinsurance amounts when they receive hospital services. In calendar year 2000, the deductible amount is $766 per spell of illness, and beneficiaries must make coinsurance payments for inpatient care in excess of 60 days and for services furnished on an outpatient basis. Before enactment of the Balanced Budget Act of 1997 (BBA), if the hospital made a reasonable effort to collect the cost-sharing amounts from patients, Medicare would reimburse it for any remaining unpaid amounts. The BBA phased in a reduction in those bad-debt payments, cutting them to 55 percent of the amount that hospitals did not collect from beneficiaries. Eliminating all reimbursement for enrollees' bad debts would reduce Medicare's payments by $500 million in 2001 and $7.4 billion over the 2001-2010 period.

This option would give hospitals incentives to improve their collection efforts, but they would not be able to collect all of the money that their Medicare patients owed. In particular, low-income enrollees who were not covered by Medicaid might not be able to pay their hospital bills. As a result, this option would reduce revenues the most for those hospitals that were most likely to serve low-income Medicare patients. Moreover, a drop in their Medicare payments might lead some hospitals to cut back on the quality of their services or the amount of uncompensated care that they provide, or to raise the rates that they charge for the care of other patients.

570-10 Eliminate Medicare's Payments to Nonhospital Providers for Enrollees' Bad Debts

	Outlay Savings (Millions of dollars)
2001	600
2002	800
2003	800
2004	900
2005	1,000
2001-2005	4,100
2001-2010	10,300

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

570-09

The Medicare program pays a variety of providers, in addition to hospitals, for the bad debts of their Medicare patients. Providers incur such debts when Medicare patients do not pay the cost-sharing amounts that the program requires. Patients in skilled nursing facilities (SNFs), for example, must pay a coinsurance amount of $97 per day in calendar year 2000 for care received from the 21st through the 100th day of a benefit period (spell of illness). (A benefit period begins with the day the beneficiary is admitted to the hospital and ends after the patient has been out of the hospital or SNF for 60 straight days, or if the beneficiary remains in the SNF after 60 straight days without receiving skilled nursing care.) Providers that are eligible for bad-debt payments include SNFs, rural health clinics, and comprehensive outpatient rehabilitation facilities. The Balanced Budget Act of 1997 reduced Medicare's payments for hospitals' bad debts but did not affect bad-debt payments for nonhospital providers. This option would eliminate such payments for nonhospital providers, saving $600 million in 2001 and $10.3 billion over the 2001-2010 period.

As with hospitals, eliminating bad-debt payments would increase providers' incentives to improve their collection efforts, but some bad debts would remain. The policy could, therefore, cause financial problems for providers that serve a large number of low-income Medicare beneficiaries. Faced with unpaid bad debts, such providers might reduce the quality of their care or the amount of uncompensated care that they provide.

570-11 Reduce Medicare Payments for Currently Covered Prescription Drugs

	Outlay Savings (Millions of dollars)
2001	200
2002	440
2003	520
2004	600
2005	700
2001-2005	2,460
2001-2010	7,230

SPENDING CATEGORY:

Mandatory

Medicare Supplementary Medical Insurance (Part B) paid providers about $4 billion in 1999 for certain outpatient drugs. Prescription drugs are covered under Part B when they must be administered under a physician's supervision, as is the case with many drugs requiring injection or infusion. Medicare also pays for drugs that must be delivered by durable medical equipment covered under the program. In addition, some oral chemotherapy and antinausea drugs for cancer patients as well as immunosuppressive drugs for organ transplant recipients are covered, as are certain vaccines.

Medicare payments for covered prescription drugs have varied over time and across settings of care. Since 1997, the amount Medicare has allowed as a reasonable charge for drugs delivered in physicians' offices and at home has been set at 95 percent of the average wholesale price, or AWP, which is a published list price established by the manufacturer. When several manufacturers make a product, the allowed charge is 95 percent of the median AWP among generic suppliers or the lowest brand-name AWP when that price is less than the median generic AWP. Medicare reimbursement for drugs delivered in hospital outpatient facilities is currently made on a cost basis, but under the Balanced Budget Act of 1997, Medicare is expected to implement a prospective payment system for hospital outpatient services beginning in July 2000. Most drugs will be exempted from the prospective payment system until at least 2002, however, and for them, the payment will be 95 percent of the AWP.

Because the AWP is a list price and not the actual price providers pay for drugs, pegging Medicare's payment to the AWP has meant that providers and suppliers could profit from administering or dispensing Medicare-covered drugs. The Inspector General of the Department of Health and Human Services reported that actual wholesale drug prices available to physicians were about 30 percent less than the AWP in 1997. This option would limit Medicare's reimbursements for prescription drugs by decreasing the allowed charge from 95 percent to 85 percent of the AWP and by limiting increases in the allowed charge for covered drugs to changes in the rate of inflation. (Changes in the allowed charge would track the consumer price index for all urban consumers, excluding food and energy.) As a result, Medicare Part B outlays would decrease by $7.2 billion between 2001 and 2010.

One disadvantage of the option is that it would encourage manufacturers to introduce new drugs at AWPs that were higher than they would otherwise be in order to restore the profit margins available to physicians and other suppliers. Physicians would prescribe newly introduced drugs more quickly as a result. Therefore, the option's effectiveness in limiting Part B spending growth would gradually erode as new drugs replaced older ones in the mix of covered drugs. Critics of the option also claim that the profit margins physicians now obtain when they administer drugs to Medicare patients subsidize the cost of drug administration, which is not now adequately reimbursed. Savings would be reduced and patient care might suffer if patients were diverted from physicians' offices to hospital outpatient settings, where Medicare reimbursements are higher. CBO's estimate includes a modest reduction in savings to account for that possibility.

570-12 Index Medicare's Deductible for SMI Services

	Outlay Savings (Millions of dollars)
2001	100
2002	290
2003	510
2004	720
2005	950
2001-2005	2,570
2001-2010	11,260

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-13-A, 570-13-B, 570-14, and 570-15

Medicare offers insurance coverage for physicians' and hospital outpatient services through the Supplementary Medical Insurance (SMI) program. The program has a number of cost-sharing requirements. One way to achieve federal savings in SMI is to increase the deductible—that is, the amount that enrollees must pay for services each year before the government shares responsibility. The deductible is now $100 a year and has been increased only three times since Medicare began in 1966, when it was set at $50. In relation to average annual per capita charges under the SMI program, the deductible has fallen from 45 percent in 1967 to about 3 percent (projected) for 2000.

Increasing the SMI deductible for 2001 and later years according to the growth in SMI charges per enrollee would save $100 million in 2001, $2.6 billion over the five-year period, and $11.3 billion over the 10-year period. In 2001, the deductible would be $108.

An increase in the amount of the deductible would enhance the economic incentives for prudent consumption of medical care while spreading the impact of an increase in cost sharing among most enrollees. No enrollee's out-of-pocket costs would rise by more than $8 in 2001.

However, the additional out-of-pocket costs under this option might discourage some low-income enrollees who are not eligible for Medicaid from seeking needed care. In addition, costs to states would increase because their Medicaid programs pay the deductibles for Medicare enrollees who also receive benefits under Medicaid.

570-13-A Simplify and Limit Medicare's Cost-Sharing Requirements

	Outlay Savings (Millions of dollars)
2001	250
2002	640
2003	770
2004	980
2005	1,260
2001-2005	3,900
2001-2010	14,690

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-13-B and 570-15

RELATED CBO PUBLICATION:

Restructuring Health Insurance for Medicare Enrollees (Study), August 1991.

Medicare's cost-sharing requirements in its fee-for-service sector are varied and difficult for beneficiaries to understand. Moreover, in contrast to most private insurance plans, Medicare places no limit on the cost-sharing expenses for which enrollees may be liable. As a result, most fee-for-service enrollees seek supplementary coverage (either through their employers or by purchasing individual medigap plans) to protect them from the potentially catastrophic expenses they might be left with under Medicare. Those enrollees with the nearly first-dollar coverage that medigap plans provide no longer have financial incentives to use medical services prudently. Consequently, Medicare's costs are higher than they would be if there were no medigap supplements.

Medicare could simplify and limit cost-sharing requirements in the fee-for-service sector while also reducing federal costs. For example, the current complicated mix of cost-sharing requirements could be replaced with a single deductible, a uniform coinsurance rate of 20 percent for amounts above the deductible, and a cap on each beneficiary's total cost-sharing expenses—whether they arose from Part A or Part B of the Medicare program. If those provisions were in place beginning in January 2001 with a deductible of $800 and a cap on total cost sharing of $2,000, federal savings would be $0.3 billion for 2001, $3.9 billion over five years, and $14.7 billion over 10 years. Those estimates assume that both the deductible and the cap would be indexed to growth in per capita benefits paid by Medicare.

For three reasons, such changes in Medicare's cost-sharing requirements would increase the incentives for enrollees to use medical services prudently. First, because about 40 percent of the medigap plans purchased do not now cover the deductible, more of the services used by those policyholders would be exempt from medigap coverage under Medicare's higher deductible. Second, over time, fewer enrollees would purchase medigap plans because their cost-sharing expenses would be capped under Medicare. Third, the uniform coinsurance rate on all services would encourage enrollees without supplementary coverage to consider relative costs appropriately when choosing among alternative treatments.

Although this option would generally reduce out-of-pocket costs for enrollees who had serious illnesses or were hospitalized during the year, it would increase out-of-pocket costs for most enrollees. On average, enrollees' cost-sharing expenses under Medicare would increase by about $45 a year in 2001. Expenses would fall for about 10 percent of enrollees, rise for about 70 percent, and be unchanged for all others. The option would also introduce cost-sharing requirements for services—such as home health care—that are not now subject to them, increasing administrative costs for the affected providers.

570-13-B Restrict Medigap Coverage

	Outlay Savings (Millions of dollars)
2001	2,190
2002	4,410
2003	4,960
2004	5,460
2005	6,060
2001-2005	23,080
2001-2010	63,500

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-12, 570-13-A, 570-15, and 570-16

RELATED CBO PUBLICATION:

Restructuring Health Insurance for Medicare Enrollees (Study), August 1991.

Savings from option 570-13-A could be substantially increased by restricting or prohibiting medigap coverage in addition to changing Medicare's cost-sharing provisions. Alternatively, some or all of the additional savings from restricting medigap coverage could be used to improve Medicare's coverage by reducing the deductible or cap.

If, for example, medigap plans were prohibited from covering any part of Medicare's new deductible (as discussed in option 570-13-A), savings would be $23.1 billion over five years and $63.5 billion over 10 years. By raising Medicare's deductible and prohibiting medigap plans from covering it, the incentives for more prudent use of health care services would be appreciably strengthened for enrollees who now have medigap plans. Those incentives would be still greater if medigap coverage was prohibited altogether. However, despite Medicare's new copayment cap, which would protect enrollees against very large cost-sharing expenses, some enrollees would object to any policy that denied them access to first-dollar coverage.

570-14 Collect Deductible and Coinsurance Amounts on Clinical Laboratory Services Under Medicare

	Outlay Savings (Millions of dollars)
2001	490
2002	1,000
2003	1,120
2004	1,210
2005	1,320
2001-2005	5,140
2001-2010	13,880

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-12 and 570-15

Medicare currently pays 100 percent of the approved fee for clinical laboratory services provided to enrollees. Medicare's payment is set by a fee schedule, and providers must accept that fee as full payment for the service. For most other services provided under Medicare's Supplementary Medical Insurance (SMI) program, beneficiaries are subject to both a deductible and a coinsurance rate of 20 percent.

Imposing the SMI program's usual deductible and coinsurance requirements on laboratory services would yield appreciable savings. If this policy was in place beginning on January 1, 2001, federal savings would be $490 million in 2001, $5.1 billion over five years, and $13.9 billion over 10 years.

In addition to reducing Medicare's costs, this option would make cost-sharing requirements under the SMI program more uniform and therefore easier to understand. Moreover, enrollees might be somewhat less likely to undergo laboratory tests with little expected benefit if they paid part of those costs.

However, enrollees' use of laboratory services would probably not be substantially affected because decisions about what tests are appropriate are generally left to physicians, whose judgments do not appear to depend on enrollees' cost-sharing liabilities. Hence, the Congressional Budget Office assumes that a small part of the expected savings under this option would stem from more prudent use of laboratory services, but the greater part would reflect the transfer to enrollees of costs now borne by Medicare. Billing costs for some providers, such as independent laboratories, would be higher under the option because they would have to bill both Medicare and enrollees to collect their full fees. (Currently, they have no need to bill enrollees directly for clinical laboratory services.) In addition, states' Medicaid costs would increase for enrollees who also received Medicaid benefits.

570-15 Impose a Copayment Requirement on Home Health Visits Under Medicare

	Outlay Savings (Millions of dollars)	
	With $5 Copayment	With $10 Copayment
2001	570	1,050
2002	1,110	2,040
2003	1,270	2,320
2004	1,430	2,600
2005	1,600	2,920
2001-2005	5,980	10,930
2001-2010	17,160	31,100

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-12, 570-13-A, 570-13-B, and 570-14

The use of home health services and the resulting costs are growing rapidly under Medicare. One reason for the unrestrained growth of such costs is that the services are free to enrollees—enrollees are not currently required to pay any portion of the cost of home health services under Medicare.

If a copayment of $5 was required for each home health visit covered by Medicare beginning in January 2001, net federal savings would be $0.6 billion in 2001, $6.0 billion over five years, and $17.2 billion over 10 years. If the copayment was $10, five-year savings would be $10.9 billion and 10-year savings would be $31.1 billion. Those estimates assume that the copayment would be indexed to the consumer price index after 2001.

This option would reduce Medicare's costs for home health care not only by shifting a small part of the cost per visit to users but also by reducing enrollees' use of the service—at least among the 15 percent of fee-for-service enrollees with no supplementary coverage for their cost-sharing expenses. However, little or no drop in use would be expected among the 85 percent of enrollees who have either Medicaid, medigap, or employment-sponsored supplementary coverage. Further, the option would increase private insurance premiums for the 35 percent of enrollees with medigap supplements, and it would increase Medicaid program costs on behalf of the 15 percent of enrollees who also receive Medicaid benefits. Moreover, it would increase the risk of very large out-of-pocket costs for those with no supplementary coverage.

570-16 Prohibit First-Dollar Coverage Under Medigap Policies

	Outlay Savings (Millions of dollars)
2001	3,780
2002	7,360
2003	8,230
2004	8,870
2005	9,570
2001-2005	37,810
2001-2010	98,030

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

570-13-B

RELATED CBO PUBLICATION:

Restructuring Health Insurance for Medicare Enrollees (Study), August 1991.

About 35 percent of Medicare's fee-for-service enrollees purchase individual supplementary private insurance (medigap coverage) that covers all or most of the cost sharing that the Medicare program requires. On average, medigap policyholders use at least 25 percent more services than they would if they did not have first-dollar coverage. However, the federal government through Medicare and not medigap insurers pays most of the costs of those additional services.

Federal costs for Medicare could be reduced if medigap plans were prohibited from offering first-dollar coverage for Medicare's cost-sharing requirements. If, for example, medigap plans were barred from paying any portion of the first $1,500 of an enrollee's cost-sharing liabilities for calendar year 2001, use of medical services by medigap policyholders would fall and federal savings in 2001 would total $3.8 billion. Assuming that the medigap limit was linked to growth in the average value of Medicare's costs for later years, savings over the 2001-2005 period would total $37.8 billion. Over 10 years, savings would total $98.0 billion.

Only enrollees who have medigap policies would be directly affected by this option, and most of them would be financially better off under it. Because their medigap premiums would decrease more than their out-of-pocket liabilities would increase, most medigap enrollees would have lower yearly expenses under this approach. Indirectly, all enrollees might be better off because Medicare's premiums would be lower than under current law.

Medigap policyholders, however, would have to assume a higher level of financial risk for Medicare-covered services than they do now. Because they might feel more uncertain about their expenses, some policyholders might object to eliminating their option to purchase first-dollar coverage, even if in most years they would be financially better off. Moreover, in any given year, about a quarter of people with medigap policies would actually incur higher expenses under this option, and those with expensive chronic conditions might be worse off year after year. Finally, the decrease in use of services by medigap policyholders that would generate federal savings under this option might not be limited to unnecessary care, so the health of some policyholders might be adversely affected.

570-17 Increase the Premium for SMI Services Under Medicare to 30 Percent of Program Costs

	Outlay Savings (Millions of dollars)
2001	2,920
2002	4,350
2003	4,810
2004	5,340
2005	5,870
2001-2005	23,290
2001-2010	60,940

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

570-18

Benefits under Medicare's Supplementary Medical Insurance (SMI) program are partially funded by monthly premiums paid by enrollees, with the remainder funded by general revenues. Although the SMI premium was initially intended to cover 50 percent of the cost of benefits, premium receipts between 1975 and 1983 covered a declining share of SMI costs—falling from 50 percent to less than 25 percent. That drop occurred because premium increases were limited by the cost-of-living adjustment (COLA) for Social Security benefits (which is based on the consumer price index) but the per capita cost of the SMI program rose faster. Since 1984, premiums have been set to cover about 25 percent of average benefits for an aged enrollee, a provision that was made permanent in the Balanced Budget Act of 1997.

If the SMI premium was set to cover 30 percent of costs for 2001 and all years thereafter, outlay savings would be $2.9 billion in 2001, $23.3 billion over five years, and $60.9 billion over 10 years. The premium for 2001 would be $59.10 a month instead of $49.30. Those estimates assume a continuation of the current hold-harmless provision, which ensures that no enrollee's monthly Social Security benefit will fall as a result of the Social Security COLA (which is based on the whole benefit) being smaller than the SMI premium increase.

Most SMI enrollees would pay a little more under this option, in contrast to proposals—such as increasing cost-sharing requirements—that could substantially raise the out-of-pocket costs of those who become seriously ill. This option need not affect enrollees with income below 120 percent of the federal poverty threshold because all of them are eligible to have Medicaid pay their Medicare premiums. (Some people who are eligible for Medicaid do not apply for benefits, however.)

Low-income enrollees who are not eligible for Medicaid could find the increased premium burdensome. A few might drop SMI coverage and either do without care or turn to sources of free or reduced-cost care, which could increase demands on local governments. In addition, states' expenditures would rise because states would pay part of the higher premium costs for those Medicare enrollees who also receive Medicaid benefits.

570-18 Tie the Premium for SMI Services Under Medicare to Enrollees' Income

	Outlay Savings (Millions of dollars)
2001	480
2002	1,670
2003	1,890
2004	2,190
2005	2,530
2001-2005	8,760
2001-2010	28,180

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-17 and REV-16

RELATED CBO PUBLICATIONS:

The Medicare Catastrophic Coverage Act of 1988 (Staff Working Paper), October 1988.

Subsidies Under Medicare and the Potential for Disenrollment Under a Voluntary Catastrophic Program (Study), September 1989.

Instead of increasing the basic premium to 30 percent of costs for all enrollees in the Supplementary Medical Insurance (SMI) program (see option 570-17), this option would collect relatively more from higher-income people. For example, people with modified adjusted gross income of less than $50,000 and couples with income lower than $75,000 would pay only the basic premium, set at 25 percent of SMI costs per aged enrollee. Premiums would rise progressively for higher-income enrollees, however. The maximum total premium would be set to cover 50 percent of costs for people with income exceeding $100,000 and for couples with income exceeding $150,000. The income-related premiums would have to be collected through the income tax system so that rates could be aligned with income. Current premiums are deducted automatically from Social Security checks for most enrollees.

If this option was in place in calendar year 2001, savings would total $480 million in fiscal year 2001, $8.8 billion over five years, and $28.2 billion over 10 years. Those estimates assume that the current hold-harmless provisions would continue only for people subject to the basic 25 percent premium. (The hold-harmless provisions ensure that no enrollee's Social Security check will decrease because an increase in the SMI premium exceeds the cost-of-living adjustment.)

Most SMI enrollees would be unaffected by tying a portion of the program's premium to income. Roughly 86 percent of enrollees would face the basic 25 percent premium, about 3 percent would pay the maximum premium, and 11 percent would pay a premium somewhere in between.

Enrollees subject to the income-related premium would pay substantially more, however. The maximum monthly premium for 2001 would be $98.60 instead of the $49.30 premium projected under current law. That increase might lead some enrollees to drop out, although it is estimated that fewer than 0.5 percent would do so. Those enrollees with retirement health plans that do not require Medicare enrollment (mainly, retired government employees) would be most likely to drop out. Some healthy enrollees who have no other source of health insurance might do so as well, if they were not averse to the risk that they might incur large health care costs.

570-19-A Increase Medicare's Age of Eligibility to Match Social Security's Normal Retirement Age

	Outlay Savings (Millions of dollars)
2001	0
2002	0
2003	390
2004	1,060
2005	1,790
2001-2005	3,240
2001-2010	29,530

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-19-B and REV-16

RELATED CBO PUBLICATION:

Long-Term Budgetary Pressures and Policy Options (Report), May 1998, Chapter 4.

Under current law, the normal retirement age (NRA) for Social Security will gradually increase from 65 to 67 in the first quarter of the next century. However, eligibility for Medicare based on age will remain at 65. Because the two programs affect the same population and because eligibility is based on the same work history, some people have argued that the age requirements should be the same.

If the age at which a person became eligible for Medicare was raised in step with increases in the NRA for Social Security, the first cohort to be affected would be people who turned 65 in 2003—for that group, eligibility for Medicare would be delayed by two months. The age of eligibility would be increased by an additional two months each year through 2008 and then remain at 66 for 12 years. Beginning in 2020, the age of eligibility would again increase by two months a year until it reached 67 in 2025. Under that option, federal budget savings would total $390 million in 2003, $3.2 billion through 2005, and $29.5 billion through 2010. Reduced spending for Medicare would be partially offset by increased spending under Medicaid, the Federal Employees Health Benefits program, and the Civilian Health and Medical Program of the Uniformed Services (reflected in the savings estimates). In addition, off-budget outlays for Social Security would fall by $8.5 billion over the 10-year period because some people who were affected would delay retirement. (That drop in costs is not reflected in the estimates.)

The same reasons that have been used to justify increasing the NRA for Social Security apply to this option as well. Life expectancy has increased substantially since Social Security and Medicare began, and a majority of workers now live well beyond the age of eligibility. When Social Security was established in 1935, average life expectancy at birth was less than 65 years; now average life expectancy is greater than 75 years. Unless changes are made in those programs, longer expected lifetimes, together with the population bulge of the baby-boom generation, will increase costs enormously under Social Security and Medicare after 2010. Only three general options for change are available: reduce the number of people eligible for benefits, reduce benefits per eligible person, or increase taxes. As a practical matter, it is likely that all three options will be called into play.

However, about 70 percent of Social Security beneficiaries retire before the normal retirement age—generally at Social Security's early retirement age of 62, which entitles them to benefits at a reduced level. Increasing Medicare's age of eligibility would also raise the number of years during which early retirees would be at risk of having no health insurance—just when their need for health care would be expected to increase significantly and their access to private individual insurance would be limited.

570-19-B Permit Early Buy-In to Medicare and Increase the Normal Age of Eligibility

	Outlay Savings (Millions of dollars)
2001	-30
2002	-390
2003	-60
2004	540
2005	1,210
2001-2005	1,270
2001-2010	23,830

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

570-19-A and REV-16

RELATED CBO PUBLICATIONS:

An Analysis of the President's Budgetary Proposals for Fiscal Year 1999 (Report), March 1998, Appendix B.

Long-Term Budgetary Pressures and Policy Options (Report), May 1998, Chapter 4.

One way to alleviate the problem that early retirees may have in continuing health insurance coverage until they are eligible for Medicare would be to introduce an early age of eligibility (62) for nondisabled retirees. (Disabled people are already eligible for Medicare regardless of their age.) That change would make the conditions for age-based eligibility under Medicare wholly consistent with those for Social Security.

Allowing people to "buy in" to Medicare at age 62 beginning in January 2001, together with the gradual move to a later normal age of eligibility (67) described in option 570-19-A, would reduce federal costs by $1.3 billion over the 2001-2005 period and by $23.8 billion through 2010. Social Security costs would increase in the early years when only the buy-in was in place, but (off-budget) savings would occur after 2004 as delays in retirement due to the increase in the eligibility age for Medicare more than offset earlier retirement among those taking advantage of the buy-in option. Those estimates assume that people who used the early buy-in option would pay an actuarially fair premium for their age group during the buy-in years. The estimates also assume that once buy-in participants reached the normal age of eligibility, they would pay a premium surcharge to compensate for any excess costs incurred during their buy-in years. (Buy-in participants are likely to be more costly to Medicare than the average person in their age group.)

600

Income Security

Budget function 600 covers federal income-security programs that provide cash or in-kind benefits to individuals. Some of those benefits (such as food stamps, Supplemental Security Income, Temporary Assistance for Needy Families, and the earned income tax credit) are means-tested, whereas others (such as unemployment compensation and Civil Service Retirement and Disability payments) do not depend on a person's income or assets. CBO estimates that in 2000, federal outlays under function 600 will total $248.9 billion, including $42.2 billion in discretionary outlays. Early in the past decade, discretionary spending in function 600 grew significantly; since then, annual growth has been much slower.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	18.9	29.6	30.4	31.9	33.1	27.5	27.8	22.7	29.7	32.7	29.7
Outlays											
Discretionary	23.5	25.8	28.2	31.3	35.7	39.2	38.0	39.4	40.9	40.0	42.2
Mandatory	123.6	144.6	168.8	175.9	178.4	181.3	188.0	191.5	192.3	197.8	206.7
Total	147.1	170.3	197.0	207.3	214.1	220.5	226.0	230.9	233.2	237.7	248.9
Memorandum:											
Annual Percentage Change in Discretionary Outlays		9.5	9.6	11.1	13.9	9.8	-3.1	3.8	3.7	-2.3	5.6

600-01 End Trade Adjustment Assistance

	Savings (Millions of dollars) Budget Authority	Outlays
2001	250	155
2002	335	320
2003	320	320
2004	320	320
2005	330	330
2001-2005	1,555	1,445
2001-2010	3,305	3,195

SPENDING CATEGORY:

Mandatory

The Trade Adjustment Assistance (TAA) program offers income-replacement benefits, training, and related services to workers who are unemployed as a result of import competition. To obtain assistance, such workers must petition the Secretary of Labor for certification and then meet other eligibility requirements. Cash benefits are available to certified workers receiving training but only after their unemployment insurance benefits are exhausted.

Ending the TAA program would reduce federal outlays by about $150 million in 2001 and by $3.2 billion during the 2001-2010 period. Affected workers could apply for benefits under the Workforce Investment Act of 1998 (WIA), which authorizes a broad range of employment and training services for displaced workers regardless of the cause of their job loss. (Because funding for WIA is limited, however, TAA cash benefits alone could be eliminated, and the remaining TAA funds for training and related services could be shifted to WIA. Doing so would reduce the total savings by about one-quarter during the 10-year period.)

The rationale for this option is to secure under federal programs more equivalent treatment of workers who are permanently displaced as a result of changing economic conditions. Since WIA provides cash benefits only under limited circumstances, workers who lose jobs because of foreign competition are now treated more generously than workers who are displaced for other reasons.

Eliminating TAA cash benefits would, however, cause economic hardship for some of the long-term unemployed who would have received them. In addition, TAA now compensates some of the workers adversely affected by changes in trade policy. Some people argue, therefore, that eliminating TAA benefits could lessen political support for free trade, which benefits the overall economy.

600-02 End the Expansion of Programs for Building New Housing Units for Elderly and Disabled People

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	811	0
2002	811	10
2003	811	115
2004	811	290
2005	811	515
2001-2005	4,055	930
2001-2010	8,110	4,695
Relative to WIDI		
2001	825	0
2002	840	10
2003	850	115
2004	865	300
2005	880	530
2001-2005	4,265	955
2001-2010	8,900	4,990

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

370-11

Since the early 1980s, federal activities to provide rental subsidies for low-income people have shifted sharply from constructing low-income housing to using less costly existing housing subsidized with vouchers and certificates. Two construction programs under which new commitments are still being made are the Section 202 and Section 811 programs for elderly and disabled people, respectively. For 2000, $811 million was appropriated to construct up to 9,400 new units and subsidize their operating costs. (The appropriation allows as much as $50 million of those funds to be used for vouchers for disabled people.)

Eliminating funding for additional new units under those programs would reduce outlays by $4.7 billion over the 2001-2010 period. Initially, savings in outlays would be substantially smaller than savings in budget authority because of the long lags involved in building new projects and thus in spending authorized funds.

Proponents of this option see little need to subsidize any new construction. The overwhelming housing problem today, they argue, is not a shortage of rental units but the inability of low-income households to afford those that exist. For example, average overall annual vacancy rates have consistently exceeded 7 percent since 1986. In any event, if elderly and disabled people need more housing assistance, it could be provided less expensively through vouchers or certificates.

Opponents of the option argue that national statistics on the supply of rental units mask local shortages of certain types of units. In particular, many households with an elderly or disabled person need housing that can provide special social and physical services that are not generally available. People who support subsidized construction of units for low-income elderly and disabled households also maintain that the high cost of producing such units requires the certainty of a guaranteed stream of income that only project-based subsidies can provide.

600-03 Increase Payments by Tenants in Federally Assisted Housing

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	330	170
2002	675	525
2003	1,055	905
2004	1,465	1,310
2005	1,820	1,740
2001-2005	5,345	4,655
2001-2010	15,825	15,330
Relative to WIDI		
2001	330	170
2002	675	525
2003	1,055	905
2004	1,465	1,310
2005	1,820	1,740
2001-2005	5,345	4,655
2001-2010	15,825	15,330

SPENDING CATEGORY:

Discretionary

Most lower-income renters who receive federal rental assistance are aided through various Section 8 programs or the public housing program, all of which are administered by the Department of Housing and Urban Development (HUD). Those programs usually pay the difference between 30 percent of a household's income after certain adjustments and either the actual cost of the dwelling or a payment standard. In 1999, the average federal expenditure per assisted household for all of HUD's rental housing programs combined was roughly $5,000. That amount includes both housing subsidies and fees paid to administering agencies.

This option would increase tenants' rent contributions over a five-year period from 30 percent to 35 percent of their adjusted income. Budgetary savings would total $15.3 billion over the 2001-2010 period, including $11.4 billion for Section 8 programs and $4.0 billion for public housing. (Those estimates are based on the assumption that the Congress will provide budget authority to extend the life of all commitments for housing aid that are due to expire during the 2001-2010 period.) To diminish or eliminate the impact of this change on assisted tenants, state governments—which currently contribute no funds toward the federal rental assistance programs—could be encouraged to make up some or all of the decreased federal support.

One rationale for directly involving states in housing assistance is that those programs generate substantial local benefits, such as improved quality of the housing stock. If all states paid 5 percent of the adjusted income of those tenants receiving assistance, housing costs for assisted families would not rise. Moreover, since eligibility for housing aid is determined by each area's median income, tying states' contributions to renters' incomes would ensure that lower-income states would pay less per assisted family than would higher-income states. Finally, if a state chose not to participate and consequently rent payments by its households increased to 35 percent of adjusted income, those out-of-pocket costs would still be well below the nearly 50 percent of income paid by the typical unassisted renter who is eligible for assistance.

Because not all states might make up the reduction in federal assistance, housing costs could increase for some current recipients of aid, who generally have very low incomes. This option could also cause some higher-income renters in assisted housing projects to move to unassisted housing because it might now cost less to rent. As those tenants were replaced by new ones with lower income, the concentration of families with very low income in those projects would increase. In turn, the savings from this option could decrease somewhat.

600-04 Reduce Rent Subsidies to Certain One-Person Households

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	35	20
2002	70	55
2003	105	85
2004	135	120
2005	170	155
2001-2005	510	430
2001-2010	1,805	1,665
Relative to WIDI		
2001	35	20
2002	70	55
2003	105	85
2004	135	120
2005	170	155
2001-2005	510	430
2001-2010	1,805	1,665

SPENDING CATEGORY:

Discretionary

Generally, recipients of federal housing aid live in housing units that are specifically designated for use by federally assisted tenants, or they rent units of their own choosing in the private rental market. Support for that second type of aid comes in the form of Section 8 certificates and vouchers, which generally reduce what recipients spend for housing to 30 percent of their income. Starting in 2000, the certificate and voucher programs will be combined into one program that will pay the difference between 30 percent of a tenant's income and the lesser of the tenant's actual housing cost or a payment standard determined by local rental levels.

The payment standard and the amount of the federal subsidy both vary according to the type of unit in which the tenant resides. One-person households may generally reside in apartments with up to one bedroom, whereas larger households may reside in larger units. Linking the rent subsidy for a newly assisted one-person household (or a currently assisted household that moves to another housing unit) to the cost of an efficiency apartment rather than a one-bedroom apartment would save $20 million in federal outlays in 2001 and nearly $1.7 billion over the 2001-2010 period.

An argument in favor of this option is that an efficiency unit would provide adequate living space for a person who lived alone. An argument against the option is that individuals in some areas might have difficulty finding suitable housing under this new rule and as a result might have to spend more than 30 percent of their income to pay for available housing.

600-05 Stop Expansion of the Number of Rental Assistance Commitments

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	345	5
2002	700	180
2003	1,060	535
2004	1,425	895
2005	1,795	1,265
2001-2005	5,325	2,875
2001-2010	20,090	14,940
Relative to WIDI		
2001	355	5
2002	715	185
2003	1,095	540
2004	1,485	915
2005	1,885	1,295
2001-2005	5,535	2,940
2001-2010	21,470	15,630

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

370-11

Each year between 1975 and 1995, and again in 1999 and 2000, the Congress expanded the stock of Section 8 certificates and vouchers to increase the number of low-income renters who receive housing aid. Those forms of housing assistance provide subsidies that allow recipients to live in private housing of their own choosing, provided the units meet certain standards. At the end of 1999, a total of about 1.6 million commitments for rental assistance were outstanding in both programs, at a total cost of about $8.1 billion in that year. For 2000, the Congress authorized $347 million to fund an additional 60,000 vouchers, and the Congressional Budget Office's baseline assumes that this amount of funding for new units will also be appropriated for each year in the future.

Stopping expansion of the number of rental assistance commitments would reduce federal outlays by $14.9 billion over the 2001-2010 period. (That estimate is based on the additional assumption that the Congress will provide budget authority to extend the life of all vouchers and certificates that are due to expire over the 2001-2010 period.)

An argument in favor of this option is that expanding rental assistance programs is inappropriate in light of the cutbacks that have occurred in other areas of federal spending. Furthermore, existing commitments will continue to assist many new eligible households each year because of turnover among assisted renters. In addition, no current recipients would lose their housing assistance as a result of this option.

An argument against the option is that less than one-third of eligible renters actually receive housing assistance. If the number of commitments was frozen, the proportion of eligible renters receiving aid would fall because of continued growth in the number of eligible households. As a result, the number of eligible households with one or more housing problems—such as paying a relatively large share of income for rent or living in a physically inadequate or crowded dwelling—would probably increase.

600-06 Reduce Funding for Employment and Training in the Food Stamp Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	140	25
2002	85	35
2003	90	45
2004	90	50
2005	100	70
2001-2005	505	225
2001-2010	1,045	750

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

600-07

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA) established a new work and training requirement for certain food stamp recipients. The act limited food stamp eligibility to a maximum of three months in any 36-month period for adults not engaged in work or job training who are able-bodied, are between the ages of 18 and 50, and have no dependent children. Under PRWORA, the requirement applies unless the Secretary of Agriculture waives it for a locale because of a high level of unemployment or insufficient job opportunities.

The Balanced Budget Act of 1997 (BBA) provided certain exemptions from the PRWORA work/training requirement as well as $600 million to fund new work/training program slots. The Agricultural Research, Extension, and Education Reform Act of 1998 (P.L. 105-185) reduced work/training funds by $100 million in 1999 and $45 million in 2000.

This option would eliminate the remaining funds for work/training slots under the BBA. It would also provide additional savings in the Food Stamp program from not paying benefits to the people who would have occupied the canceled slots. In total, the Congressional Budget Office estimates that the option would reduce outlays by $25 million in 2001 and about $750 million for the 2001-2010 period.

An argument for eliminating the remaining work/training funds provided under the BBA is that states have not been using all of the funds allotted to them. States receive basic federal funding for employment and training of food stamp recipients under the Food Stamps Act of 1985, and those funds can be used for able-bodied adults without dependent children. People facing the work/training requirement under PRWORA can also apply to other programs that operate independently of the Food Stamp program. States with economically distressed areas, which might have fewer alternative work/training opportunities than more prosperous locales, can also apply for waivers from the PRWORA requirement.

An argument against this option is that the unspent funds are not necessarily evidence of a lack of need. States have had little time to develop the work/training programs that the BBA authorizes. Such programs must be targeted primarily at able-bodied adults without dependent children and may not simply substitute for state-funded programs. To ensure that BBA funds are spent on new work/training efforts, the act requires states to maintain their 1996 state spending levels for work/training programs in order to collect the BBA funds. Another argument for maintaining the funds available under the BBA is that they offer some flexibility because they do not have to be spent in a particular fiscal year. The funds may be carried over and reallocated by the Secretary of Agriculture among the states on the basis of year-to-year changes in the distribution of covered individuals.

600-07 Reduce the Exemptions from Employment and Training Requirements for Food Stamp Recipients

	Savings (Millions of dollars) Budget Authority	Outlays
2001	30	30
2002	30	30
2003	30	30
2004	30	30
2005	35	35
2001-2005	155	155
2001-2010	340	340

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

600-06

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA) is intended to encourage people to work or pursue job training. Thus, the act restricts food stamp eligibility to a maximum of three months in any 36-month period for able-bodied adults not engaged in work or training who are 18 to 50 years of age and have no dependent children—unless the Secretary of Agriculture has waived the work/training requirement for their locale. Under the Balanced Budget Act of 1997 (BBA), however, states may exempt from the requirement up to 15 percent of such able-bodied food stamp recipients.

This option would eliminate the 15 percent exemption to the PRWORA work/training requirement, which the Congressional Budget Office estimates would reduce outlays by $30 million in 2001 and $340 million for the 2001-2010 period.

The BBA exemption allows states to use different food stamp eligibility rules for different childless adults. Eliminating the exemption would require states to use the same eligibility criteria for all 18- to 50-year-old able-bodied people with no dependent children who live in a particular local area. An argument against this option is that the exemption provides a safety net for a needy population that can be difficult to serve.

600-08 Reduce the $20 Unearned Income Exclusion Under the Supplemental Security Income Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	90	90
2002	120	120
2003	120	120
2004	125	125
2005	135	135
2001-2005	590	590
2001-2010	1,225	1,225

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

600-09

The Supplemental Security Income (SSI) program provides federally funded monthly cash payments—based on uniform, nationwide eligibility rules—to low-income elderly and disabled people. In addition, most states provide supplemental payments. Because SSI is a means-tested program, recipients' outside income reduces their SSI benefits, subject to certain exclusions. For unearned income, most of which is Social Security, $20 a month is excluded; benefits are reduced dollar for dollar for unearned income above that amount. The program allows a more liberal exclusion for earned income in order to maintain work incentives.

This option would reduce the monthly $20 unearned income exclusion to $15. The Congressional Budget Office estimates that the savings from that change would be $90 million in 2001 and $1.2 billion over the 2001-2010 period.

A program that ensures a minimum living standard for its recipients need not provide a higher standard for people who happen to have unearned income. Nevertheless, reducing the monthly $20 exclusion by $5 would decrease by as much as $60 a year the incomes of the roughly 2.5 million low-income people (approximately 40 percent of all federal SSI recipients) who would benefit from the exclusion in 2001. Even with the full $20 exclusion, the incomes of most SSI recipients fall below the poverty threshold.

600-09 Create a Sliding Scale for Children's SSI Benefits Based on the Number of Recipients in a Family

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	55	55
2003	120	120
2004	130	130
2005	150	150
2001-2005	455	455
2001-2010	1,255	1,255

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

600-08

The Supplemental Security Income (SSI) program provides cash payments—based on uniform, nationwide eligibility rules—to elderly and disabled people with low incomes. In addition, most states provide supplemental payments to SSI recipients. In 1999, children received approximately $4.9 billion in federal SSI benefits, accounting for almost one-sixth of federal SSI benefits paid that year.

Unlike other means-tested benefits, the amount of the SSI benefit for an additional child does not decline as the number of SSI recipients in a family increases. In 2000, a family with one child qualifying for SSI benefits could receive up to $512 a month, or $6,144 a year, if the family's income (excluding SSI benefits) was under the cap for the maximum benefit. If the family had additional eligible children, it could receive an additional $512 a month for each one. (A child's benefit is based only on the presence of a severe disability and the family's income and resources, not on the nature of the qualifying disability or on participation by other family members in the SSI program.)

This option would create a sliding scale for SSI disability benefits, so that a family would receive smaller benefits per child as the number of children receiving SSI increased. The sliding scale used for this option was recommended by the National Commission on Childhood Disability in 1995. It would keep the maximum benefit for one child as it is in current law but reduce additional benefits for additional recipient children in the same family. If that sliding scale was in place in 2000, the first child in a family qualifying for the maximum benefit would receive $512, the second child would receive $320 (38 percent less), and the third would receive $273 (47 percent less). Benefits would continue to decrease for additional children. About 90 percent of child recipients would be unaffected by the new scale, and the remaining 10 percent would have their benefits reduced by about one-fourth, on average. As with current SSI benefits, the sliding scale would be adjusted each year to reflect changes in the consumer price index.

The Congressional Budget Office assumes that this option would not be implemented until 2002, because the Social Security Administration does not maintain data on multiple SSI recipients in a family and implementation of the sliding scale would therefore require significant effort. Savings from this option would total $55 million in 2002 and $1.26 billion over the 2002-2010 period.

Proponents of this option argue that the proposed reductions in benefits reflect economies of scale that generally affect the cost of living for families with more than one child. Proponents might also note that the high medical costs that disabled children often incur, which would not be subject to economies of scale, would continue to be covered because SSI participants generally are covered by Medicaid. Still, opponents could argue that children with disabilities sometimes have unique needs that may not be covered by Medicaid, including housing modifications and specialized equipment. With the proposed drop in benefits, some families might be unable to meet such needs.

600-10 Reduce the Federal Matching Rate for Administrative Costs in the Child Support Enforcement Program

	Savings (Millions of dollars) Budget Authority	Outlays
2001	980	980
2002	1,070	1,070
2003	1,160	1,160
2004	1,260	1,260
2005	1,350	1,350
2001-2005	5,820	5,820
2001-2010	14,070	14,070

SPENDING CATEGORY:

Mandatory

The Child Support Enforcement (CSE) program, enacted in 1975, assists states in their effort to improve the payment of child support by noncustodial parents. The federal government pays 66 percent of the program's administrative costs, provides incentive payments, and allows states to retain some of the money they collect.

This option would reduce the federal share of administrative costs from 66 percent to 50 percent. The Congressional Budget Office estimates that lowering the federal matching rate could save $980 million in 2001 and $14.1 billion through 2010.

Several arguments can be made for shifting greater responsibility for CSE administrative costs to the states. For one thing, it would encourage states to make their CSE efforts more efficient because states would be paying a larger share of the costs of any inefficiencies. Moreover, it would bring the federal share of CSE administrative costs more in line with the share of such costs that the federal government bears in comparable programs.

Lowering the matching rate would entail some risks, however. Because caseloads for child support workers are already high, states are not likely to be able to improve the program's efficiency enough to offset the reduction in federal payments. As a result, states might cut their CSE services, and child support collections might drop. A reduction in collections could also mean higher state costs for Temporary Assistance for Needy Families (TANF) because state collections of child support partly offset states' TANF benefit payments. States might respond to their greater share of the costs by reducing their benefits and services for needy families.

Under the Unfunded Mandates Reform Act of 1995, reductions in federal funding for certain entitlement grant programs—including the Child Support Enforcement program—are considered mandates on state governments if the states lack authority to amend their programmatic or financial responsibilities to offset the loss of funding. Because some states may not have sufficient flexibility within the CSE program to make such changes, this option could constitute an unfunded mandate on those jurisdictions under the law.

600-11 Reduce TANF Block Grants to States

	Savings (Millions of dollars) Budget Authority	Outlays
2001	819	75
2002	819	75
2003	814	110
2004	799	365
2005	769	775
2001-2005	4,020	1,400
2001-2010	7,820	6,125

SPENDING CATEGORY:

Mandatory

Under the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), the federal government provides block grants to states for Temporary Assistance for Needy Families (TANF). The amounts of the block grants are based on spending levels for three programs that PRWORA repealed and TANF replaces: Aid to Families with Dependent Children (AFDC), Emergency Assistance for Needy Families, and the Job Opportunities and Basic Skills (JOBS) training program. To receive TANF funds, a state must spend from its own funds a predetermined "maintenance-of-effort" amount based on its pre-TANF spending. In addition, the state must maintain minimum work participation rates for recipient families, require parents and caretaker recipients to engage in work activities after receiving no more than 24 months of TANF benefits (with some exemptions), and impose a five-year limit on receipt of federally funded TANF benefits. Currently, the Congress has authorized $16.5 billion annually for TANF through 2002.

This option would reduce the TANF block grants to states by 5 percent, which the Congressional Budget Office estimates would reduce budget authority by $819 million and outlays by $75 million in 2001. For 2001 to 2010, CBO estimates that this option would reduce budget authority by $7.8 billion and outlays by $6.1 billion.

Budget authority is projected to fall by less than the full 5 percent reduction in the TANF block grant because of the increase in spending for food stamps that would occur when TANF benefits were reduced. Outlays would initially fall by less than the reduction in budget authority because caseloads in the AFDC and TANF programs have declined significantly over the past six years and many states have been accumulating TANF budget authority from their current annual block grants. The cut in budget authority would result in lower outlays only after a state had depleted its stored budget authority.

An argument for reducing the TANF block grants is that most states need much less money for their programs than legislators expected when PRWORA was enacted. An argument against the cut is that it would reduce federal spending immediately in several states that have been exhausting their TANF block grants, which could cause those states to cut their TANF benefits and services. In addition, reducing federal funding could be viewed as an abrogation of a prior agreement between the federal and state governments and could make future agreements on block grants more difficult.

600-12 Reduce Funding for the Low Income Home Energy Assistance Program

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	110	85
2002	110	110
2003	110	110
2004	110	110
2005	110	110
2001-2005	550	525
2001-2010	1,100	1,075
Relative to WIDI		
2001	110	85
2002	125	120
2003	145	140
2004	165	160
2005	185	180
2001-2005	730	685
2001-2010	1,970	1,895

SPENDING CATEGORY:

Discretionary

The Low Income Home Energy Assistance Program (LIHEAP) helps some low-income households pay their home energy costs. Authorized by the Omnibus Budget Reconciliation Act of 1981 and distributed through block grants to the states, LIHEAP funding is $1.1 billion in 2000. States may use the grants to help eligible households pay home heating or cooling bills, provide energy "crisis intervention" for those in immediate need, and fund low-cost weatherization projects. Additionally, the LIHEAP appropriation includes $300 million for energy emergencies designated by the President.

Households may be eligible for the program if they receive assistance under certain means-tested programs or if their income is sufficiently low. Eligibility requirements are set by the states within federal guidelines. For example, the states may give preference to households with the highest energy costs (relative to income).

Cutting LIHEAP funding by 10 percent would save nearly $1.1 billion in federal outlays during the 2001-2010 period. (To achieve savings in 2001, the funding reduction would have to be applied to funds that have already been appropriated.) One way of achieving that reduction in spending would be for states to forgo weatherization spending, which includes funds for new windows, doors, and furnaces that reduce future energy use. In 1996, states spent an average of just over 10 percent of their LIHEAP block grants for weatherization. Currently, states can spend up to 15 percent of their grant funds for weatherization, with the option of obtaining a waiver that allows expenditures of as much as 25 percent. Each year between 1995 and 1998, five states on average received that type of waiver.

An argument in favor of reducing LIHEAP funding is that the program was created in response to rapid increases in the price of home energy sources in the late 1970s and early 1980s. Even with their recent rise, however, real energy prices (adjusted for inflation) have decreased by almost 30 percent since 1981. In addition, the small number of waivers that states have obtained to increase weatherization spending supports the claim that most do not regard weatherization as a priority for LIHEAP funds. The federal government already provides similar assistance through the Department of Energy's (DOE's) Weatherization Assistance Program for low-income people, which has an appropriation of $135 million in 2000 and serves about 70,000 households per year.

An argument against reducing LIHEAP funding is that spending for the program has already declined. In real terms, its 2000 appropriation is about half of its first appropriation. From 1981 to 1999, the percentage of eligible households receiving assistance dropped from 36 percent to 15 percent. Moreover, many communities have yearlong waiting lists for assistance from DOE's weatherization program, making it unlikely that the DOE program would be able to make up for LIHEAP's decreased coverage. In addition, it would be impossible for all of the states to limit cuts in funding to weatherization assistance. In 1996, six states did not fund any weatherization projects. To comply with this option, those six states and others that use less than 10 percent of their grant funds for weatherization would have to cut their basic LIHEAP spending.

600-13-A Defer Cost-of-Living Adjustments for CSRS Annuitants

	Savings (Millions of dollars) Budget Authority	Outlays
2001	355	355
2002	510	510
2003	430	430
2004	520	520
2005	665	665
2001-2005	2,480	2,480
2001-2010	8,305	8,305

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

600-13-B, 600-13-C, 600-14, 600-15-A, 600-15-B, and 600-16

RELATED CBO PUBLICATION:

Comparing Federal Employee Benefits with Those in the Private Sector (Memorandum), August 1998.

Federal civilian retirement programs cover about 2.7 million active employees and 2.4 million retirees and survivors. Federal civilian pension payments totaled $44 billion in 1999. Civilian workers covered by the Civil Service Retirement System (CSRS), which covers most civilian employees hired before January 1, 1984, receive full cost-of-living-adjustments (COLAs). Civilian employees hired after that date receive less generous protection from inflation. Employees covered by the post-1983 civilian plan, the Federal Employees Retirement System (FERS), receive a so-called diet-COLA, generally 1 percentage point less than inflation. Moreover, COLAs are generally paid only to FERS retirees who are age 62 and older.

This option and options 600-13-B and 600-13-C illustrate three basic approaches to reducing the cost of COLAs: deferring adjustments for inflation, limiting the size of those adjustments, and reducing adjustments for middle- and high-income retirees. All three options would still give federal retirees better protection against inflation than private-sector pensions give to their retirees. However, as with any cut in benefits, those reductions could make recruitment and retention harder for federal civilian programs.

Deferring COLAs until age 62 for all nondisabled civilian employees who retired before that age would yield savings in direct spending of $355 million in 2001, $2.5 billion over five years, and $8.3 billion over 10 years. Consistent with the military retirement system, this option allows a one-time catch-up adjustment at age 62, increasing pensions to the amount that would have been payable had full COLAs been in effect. Under the COLA-deferral approach, a CSRS-covered annuitant retiring at age 55 with an average annuity of $25,000 in 2001 would lose $17,000 over seven years.

Deferring COLAs would align COLA practices for CSRS with those under FERS and encourage federal employees to work longer. A major disadvantage of this option is that for current retirees or those nearing retirement, it could be regarded as a revocation of earned retirement benefits. In addition, although CSRS benefits are more generous than the total package of benefits typically offered by private employers, they fall short of those offered by many large private firms, which compete directly with the federal government in labor markets. Moreover, because CSRS benefits are already less generous than those available under FERS, this option would worsen the disparity between the government's civilian retirement plans.

600-13-B Limit Some COLAs for Federal Retirees

	Savings (Millions of dollars) Budget Authority	Outlays
2001	165	165
2002	385	385
2003	610	610
2004	845	845
2005	1,080	1,080
2001-2005	3,085	3,085
2001-2010	12,135	12,135

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

600-13-A, 600-13-C, 600-14, 600-15-A, 600-15-B, and 600-16

RELATED CBO PUBLICATION:

Comparing Federal Employee Benefits with Those in the Private Sector (Memorandum), August 1998.

Annuitants under the Civil Service Retirement System (CSRS) receive annual cost-of-living adjustments (COLAs) that offer 100 percent protection against inflation. Annuitants under the Federal Employees Retirement System (FERS) receive full protection only when the annual rate of inflation is less than 2 percent. If inflation in a year is between 2 percent and 3 percent, FERS annuitants receive COLAs of 2 percent. If inflation is over 3 percent, the adjustment is the increase in inflation less 1 percentage point.

This option would limit COLAs for CSRS annuitants to half a percentage point below inflation. Moreover, when inflation fell below 3 percent, FERS retirees would receive a COLA equaling the rate of inflation less a percentage point. The smaller one-half point reduction for CSRS retirees would produce a cut roughly comparable with the 1 percentage-point limit for FERS enrollees, who are also covered by Social Security.

Savings in direct spending for civilian pensions would amount to $165 million in 2001, $3.1 billion over five years, and $12.1 billion over 10 years. Over five years, the average CSRS retiree would lose $2,200. (Savings from this option would fall by $460 million over five years if it was coupled with option 600-13-A, which would defer COLAs until age 62 for CSRS workers.) The Congress could also consider limiting COLAs only for the more generous FERS plan.

The main argument for this approach, as with the other COLA options, is that COLA protection under federal pension plans exceeds that offered by private pension plans. COLAs are becoming less prevalent in the private sector. According to a 1995 survey by the Bureau of Labor Statistics, less than 10 percent of private-sector annuitants received any inflation protection in the previous five years.

The main argument against cutting any retirement benefit is that such an action hurts both retirees and the government's ability to recruit a quality workforce. Advocates for federal workers argue that although certain provisions of federal retirement plans are generous, total compensation should be the basis of comparison between federal and private-sector employment. Annual surveys indicate that federal workers may be accepting salaries below private-sector rates for comparable jobs in exchange for better retirement provisions. In essence, workers pay for their more generous retirement benefits by accepting lower wages during their working years. This option, however, would hurt those retirees most dependent on their pensions. It would also renege on an understanding that workers covered under CSRS who passed up the chance to switch to FERS would retain their full protection against inflation. Finally, critics note that some protection from inflation for federal retirees has been restricted in the past. The General Accounting Office calculated that COLA delays and reductions during the 10-year period from 1985 through 1994 effectively reduced COLAs to about 80 percent of inflation.

600-13-C Reduce COLAs for Middle- and High-Income Federal Retirees

	Savings (Millions of dollars) Budget Authority	Outlays
2001	235	235
2002	560	560
2003	890	890
2004	1,225	1,225
2005	1,565	1,565
2001-2005	4,475	4,475
2001-2010	17,385	17,385

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

600-13-A, 600-13-B, 600-14, 600-15-A, 600-15-B, and 600-16

RELATED CBO PUBLICATION:

Comparing Federal Employee Benefits with Those in the Private Sector (Memorandum), August 1998.

Another alternative would tie reductions in the cost-of-living adjustment (COLA) to annuitants' benefit levels. For example, the full COLA could be awarded only on the first $700 of a retiree's monthly benefit; a half COLA could be given on the remainder. The average pension for a civilian retiree was $1,800 a month in 1999. The threshold of $700 per month is about equal to the projected poverty level for an elderly person in 2000 and could be indexed to maintain its value over time. Similar proposals have been considered for Social Security.

This approach would save about $235 million in direct spending for civilian pensions in 2001, $4.5 billion over the 2001-2005 period, and $17.4 billion over 10 years. The average retiree under the Civil Service Retirement System (CSRS) who was affected by the cut would lose $2,460 over five years. Because the full COLA would be paid only to beneficiaries with small annuities, this option would better focus COLAs on retirees who had the greatest need for protection from inflation. Retirees receiving Federal Employees Retirement System (FERS) benefits already receive a reduced COLA, so this change would affect them less than those receiving CSRS benefits. As a result, the option would widen the existing gap between total benefits provided by FERS—including Social Security and the Thrift Savings Plan—and those provided by CSRS, leaving FERS even more generous relative to CSRS than it had been in the past.

The disadvantage of the option is that it would reduce the ability of the federal government to hire and retain middle- and upper-level managers and professionals. In addition, restricting COLAs would undercut a major strength of the federal retirement system—its ability to offer indexed pensions. Fully indexed benefits provide insurance against inflation, which generally is not offered in the private sector. Furthermore, many people object to any reductions in earned retirement benefits. They also point out that federal pensions are fully taxable under the individual income tax in the same proportion that they exceed the contributions that employees made during their working years. Moreover, pension benefit levels are not always reliable indicators of total income. As a result, unrestricted COLAs might be paid to recipients who had substantial income from other sources.

600-14 Modify the Salary Used to Set Federal Pensions

	Savings (Millions of dollars)	
	Budget Authority	Outlays
2001	20	20
2002	55	55
2003	95	95
2004	130	130
2005	170	170
2001-2005	470	470
2001-2010	1,815	1,815

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

600-13-A, 600-13-B, 600-13-C, 600-15-A, 600-15-B, and 600-16

RELATED CBO PUBLICATION:

Comparing Federal Employee Benefits with Those in the Private Sector (Memorandum), August 1998.

Both of the government's major civilian employee retirement plans, the Federal Employees Retirement System (FERS) and the Civil Service Retirement System (CSRS), provide initial benefits based on the average salary for an employee's three highest-earning years. If a four-year average was adopted for future retirees under FERS and CSRS, initial pensions would be about 1.5 percent to 2 percent smaller for most new civilian retirees. In 2001, total savings to the government in direct spending for civilian pensions would be $20 million; savings would total $470 million over five years and $1.8 billion over 10 years.

This option would align federal practices more closely with those in the private sector, which commonly uses five-year averages. The change in figuring the base salary would encourage some employees to remain on the job longer in order to boost their pensions to reflect the higher salaries they receive with more years on the job. That incentive could help the government keep experienced people, but it would hinder efforts to reduce federal employment and promote younger hires.

The major drawback to the option is that it would cut benefits and consequently reduce the attractiveness of the government's civilian compensation packages.

Under this option, FERS benefits—including Social Security and the Thrift Savings Plan (TSP)—would remain more generous than those offered by large private firms, but CSRS benefits would fall below those received by many retirees in the private sector. The average new CSRS retiree would lose $500 in 2001 and $2,600 over five years, whereas the average new FERS retiree would lose $150 in 2001 and just $800 over five years because of the smaller defined benefit under that system. Retirees participating in FERS would continue to receive their full Social Security benefits and distributions from the TSP. In contrast, Social Security does not cover CSRS participants, and the government makes no contributions to TSP accounts established by CSRS participants.

600-15-A Restrict the Government's Matching Contributions to the Thrift Savings Plan

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	665	665
2002	700	700
2003	730	730
2004	765	765
2005	805	805
2001-2005	3,665	3,665
2001-2010	8,220	8,220
Relative to WIDI		
2001	685	685
2002	750	750
2003	815	815
2004	885	885
2005	960	960
2001-2005	4,095	4,095
2001-2010	10,110	10,110

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

600-13-A, 600-13-B, 600-13-C, 600-14, 600-15-B, and 600-16

RELATED CBO PUBLICATIONS:

Comparing Federal Employee Benefits with Those in the Private Sector (Memorandum), August 1998.

Comparing Federal Salaries with Those in the Private Sector (Memorandum), July 1997.

The Thrift Savings Plan (TSP) for federal civilian employees is a defined contribution pension plan similar to the 401(k) plans that many private employers offer. Federal agencies automatically contribute to the TSP an amount equal to 1 percent of an individual's earnings on behalf of each of the 1.5 million workers covered by the Federal Employees Retirement System (FERS). In addition, the employing agency matches voluntary deposits by employees dollar for dollar on the first 3 percent of their pay and 50 cents for each dollar on the next 2 percent. The total federal contribution is 5 percent of pay for employees who also put aside 5 percent. Employees covered by the Civil Service Retirement System (CSRS), which covers most civilian federal employees hired before January 1, 1984, can contribute 5 percent of their pay to the TSP, but agencies contribute nothing on behalf of those employees.

If the government limited its matching contributions to a uniform rate of 50 percent on the first 5 percent of pay, its maximum contribution would fall to 3.5 percent of pay. Savings from that proposal would total $665 million in 2001 and $3.7 billion over five years relative to the 2000 funding level. Ten-year savings would reach $8.2 billion. (The estimates exclude savings realized by the Postal Service because reductions in its operating costs eventually benefit only mail users.) Assuming that agencies continued the automatic 1 percent contribution, this arrangement would remain more generous than the defined contribution pension plans that are typically offered in the private sector.

Limiting the matching contributions would reduce the disparity between the government's two major retirement systems. Benefits under FERS are currently more generous than those under the older CSRS for most participants. Yet restricting the matching contributions would have several drawbacks. Middle- and upper-income employees rely on the government's contributions to maintain their standard of living during retirement because Social Security replaces a smaller fraction of their income than it does for lower-income employees. Part of the TSP's appeal derives from its individual accounts for each participant, which enjoy some protection from cuts imposed by subsequent changes in law. The security and portability of the TSP were major factors in the decision of many employees to switch from CSRS to FERS, because the TSP compensated for a less generous defined benefit plan. Changing the TSP's provisions would be unfair to that group, whose decision to switch plans reasonably assumed that changes would not be made. Opponents of restricting the matching rate also argue that doing so would diminish employees' savings for retirement, a problem that would be intensified if the cut reduced TSP participation. Research shows, however, that private-sector employees' contributions to their 401(k) plans tend to be responsive to the offer of employer matching contributions but not to the size of the match.

600-15-B Restructure the Government's Matching Contributions to the Thrift Savings Plan

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	310	310
2002	325	325
2003	340	340
2004	360	360
2005	375	375
2001-2005	1,710	1,710
2001-2010	3,835	3,835
Relative to WIDI		
2001	320	320
2002	350	350
2003	380	380
2004	415	415
2005	450	450
2001-2005	1,915	1,915
2001-2010	4,725	4,725

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

600-13-A, 600-13-B, 600-13-C, 600-14, 600-15-A, and 600-16

RELATED CBO PUBLICATIONS:

Comparing Federal Employee Benefits with Those in the Private Sector (Memorandum), August 1998.

Comparing Federal Salaries with Those in the Private Sector (Memorandum), July 1997.

Federal workers covered by the Federal Employees Retirement System (FERS) can contribute up to 10 percent of their salary into the Thrift Savings Plan (TSP), which is similar to a 401(k) plan. However, an employee can receive the highest contribution the government is willing to make to the TSP, an amount equal to 5 percent of the employee's pay, by contributing only 5 percent of earnings. Restructuring the government's contribution schedule so that the government would make the full 5 percent contribution only when employees contribute the 10 percent maximum amount would save $310 million in 2001 and $1.7 billion over five years. Ten-year savings would reach $3.8 billion.

Currently, federal agencies automatically contribute an amount equal to 1 percent of salaries into the TSP for their FERS employees. In addition, employing agencies match the first 3 percent of voluntary employee contributions dollar for dollar and the next 2 percent at 50 cents on the dollar. (Employees covered by the Civil Service Retirement System (CSRS) are not eligible for either the automatic or the matching contributions but may contribute 5 percent of pay to the TSP.)

This option would spread the government's total 5 percent contribution over the 10 percent maximum contribution for employees. It would do so by matching voluntary contributions ranging from 1 percent up to 6 percent at the rate of 50 cents per dollar (for a maximum 3 percent match), and those ranging from 7 to 10 percent at 25 cents per dollar (for a maximum 1 percent match). The government would continue to automatically contribute an amount equal to 1 percent of employee earnings.

Changing the government's matching schedule would bring the government's practices more in line with those of defined contribution plans in the private sector, which usually provide less generous matching contributions and no automatic contributions. According to the Bureau of Labor Statistics, the most prevalent practice among medium and large private firms is to match employee contributions up to 6 percent of pay at 50 cents on the dollar. Some federal employees, especially those currently contributing 5 percent of pay, would have an incentive to contribute more to the TSP and as a result would have more savings available to them when they retired. Further, restructuring matching contributions might reduce the disparity between the government's two major retirement systems. Benefits under FERS are currently higher and cost the government more than those under the older CSRS for most participants.

This option has several drawbacks, however. First, a lower government match on smaller contributions may reduce the retirement resources for some employees by weakening their incentive to contribute. Second, the government may achieve its savings at the expense of employees who are least likely to contribute a higher percentage of earnings into the TSP—namely, young workers and others with relatively low earnings. Third, changing the TSP may be considered unfair because many people accepted employment with the government or switched from CSRS to FERS based on the assumption that TSP benefits would not change.

600-16 Increase Employee Contributions for Federal Pensions

	Savings (Millions of dollars)
2001	0
2002	0
2003	925
2004	1,125
2005	1,120
2001-2005	3,170
2001-2010	8,540

CATEGORY:

Mandatory Spending and Revenues

RELATED OPTIONS:

600-13-A, 600-13-B, 600-13-C, 600-14, 600-15-A, and 600-15-B

RELATED CBO PUBLICATIONS:

Comparing Federal Employee Benefits with Those in the Private Sector (Memorandum), August 1998.

Comparing Federal Salaries with Those in the Private Sector (Memorandum), July 1997.

This option would permanently increase by 0.5 percent of pay the contributions that most federal civilian employees make to their retirement plan. Before 1999, most civilian workers covered by the Civil Service Retirement System (CSRS), the older of the two major civilian retirement plans, contributed 7 percent of their salary to their retirement fund. However, as CSRS-covered workers, they pay no Social Security taxes. Employees covered by the other major civilian plan, the Federal Employees Retirement System (FERS), generally contributed 0.8 percent of pay toward a defined benefit plan and paid 6.2 percent in Social Security taxes. The Balanced Budget Act of 1997 temporarily raises federal civilian employees' contributions to the retirement funds by 0.5 percent of pay; it also raises nonpostal agencies' contributions for CSRS participants by 1.5 percent of pay. The government began phasing in those increases in January 1999—employee contributions initially rose by 0.25 percent of pay. The increases are scheduled to expire after 2002. This option would make those higher employee and agency contributions for civilian pensions permanent.

Adopting this option for civilian employees would increase savings in mandatory programs by $3.2 billion over five years and $8.5 billion over 10 years. (The estimates assume that agencies' contributions for employees under FERS remain unchanged.)

Requiring employees to contribute to their retirement funds is one way to offset the generosity of federal civilian pension benefits relative to those in the private sector yet maintain a high level of salary replacement once people retire. On the downside, for most federal civilian employees, the option would be roughly equivalent to a 0.5 percent pay cut and would further diminish the federal government's compensation package relative to that of the private sector. (Private firms seldom require employees to contribute to pension plans.) Those factors would weaken the government's ability to attract new personnel. The government as a result might attract a less skilled workforce or be forced to raise cash compensation for its employees.

700

Veterans Benefits

Budget function 700 covers programs that offer benefits to military veterans. Those programs, most of which are run by the Department of Veterans Affairs, provide health care, disability compensation, pensions, life insurance, education and training, and guaranteed loans. CBO estimates that outlays for function 700 will total $44.8 billion in 2000, including discretionary outlays of $20.4 billion. Over the past decade, discretionary outlays for veterans' benefits have increased almost every year.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	13.0	14.1	15.3	16.2	17.2	17.6	17.8	18.9	18.9	19.3	20.9
Outlays											
Discretionary	13.0	13.8	15.1	15.8	16.7	17.4	17.6	18.6	18.5	19.4	20.4
Mandatory	16.1	17.5	19.0	19.8	20.9	20.5	19.4	20.7	23.3	23.8	24.4
Total	29.1	31.3	34.1	35.7	37.6	37.9	37.0	39.3	41.8	43.2	44.8
Memorandum:											
Annual Percentage Change in Discretionary Outlays		5.9	9.8	4.7	5.7	4.3	1.0	5.7	-0.6	4.7	5.1

700-01 Charge Monthly Rather Than Up-Front Fees for VA Mortgage Insurance

	Savings (Millions of dollars) Budget Authority	Outlays
2001	152	152
2002	137	137
2003	364	364
2004	349	349
2005	327	327
2001-2005	1,329	1,329
2001-2010	2,991	2,991

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

700-04

The Department of Veterans Affairs (VA) operates a home loan guaranty program that insures mortgages for active-duty military personnel and veterans. Borrowers taking advantage of the program pay a one-time, up-front funding fee. In contrast, borrowers using private mortgage insurance generally pay monthly fees.

This option would replace the up-front fee in the VA program with an annual premium, paid monthly, starting in 2001. Budget savings to the VA would total $1.3 billion over five years and $3 billion through 2010. Under current law, the up-front fee will decline in 2003. About half of the saving estimated for this option would come from not reducing that fee in 2003; the other half would come from the additional change to monthly premiums. Actual savings from the option, however, would depend on future economic conditions: savings could be lower if the program experienced high rates of default or high rates of refinancing to conventional loans.

Besides saving money for the VA, changing from an up-front to a monthly fee would have advantages for program participants. First, it would increase fairness among borrowers by charging them for mortgage insurance only for the years that they needed and used it. Active-duty military personnel who regularly change their duty station would pay less than they do under the current fee structure. For example, borrowers who sold their home after five years would save more than $700 (on a present-value basis) with a monthly fee, compared with a 2 percent up-front fee on a loan with no down payment. An additional element of fairness among borrowers would result because the monthly fee would cause borrowers who defaulted on their mortgage to pay significantly more toward their insurance than they do now. When the up-front fee is financed as part of the mortgage—as it typically is today—borrowers who subsequently default pay very little of the fee.

Second, the annual fee assumed in this option (0.35 percent) is significantly lower than premium rates that private mortgage insurers charge for comparable coverage. Thus, the program would continue to provide a significant benefit to military personnel.

Third, because the up-front fee is usually financed as part of the mortgage, adopting a monthly fee would reduce mortgage amounts, making it easier for borrowers to sell their homes, and thus reduce rates of default and foreclosure. Today, since most VA mortgages combine financing of the up-front fee with a zero downpayment, the program creates "upside-down" loans whose balances are greater than the underlying property values. Borrowers in that situation must wait for the price of their home to appreciate significantly before they can afford to sell it and move. If the price does not rise fast enough, default becomes a viable option when the borrower must move to a new location. The January 1999 *Report of the Congressional Commission on Servicemembers and Veterans Transition Assistance* raised concern about upside-down loans and their added risk of default.

Changing the fee structure for VA mortgage insurance could have drawbacks, however. First, the department would need to establish a system to receive monthly premium receipts from lenders, which could necessitate new accounting and computer systems. Second, the change would require borrowers to either make slightly higher monthly mortgage payments (an average of $17 higher during the years in which the premiums were due), purchase homes of lower value (an average of $2,300 lower), or some combination of the two.

700-02 End Future Veterans' Compensation Payments for Certain Veterans with Low-Rated Disabilities

	Savings (Millions of dollars)	
	Budget Authority	Outlays
2001	22	20
2002	67	64
2003	114	110
2004	163	159
2005	232	229
2001-2005	598	582
2001-2010	2,542	2,503

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

700-03

Approximately 2.3 million veterans who have service-connected disabilities receive veterans' disability compensation benefits. The amount of compensation is based on a rating of the individual's impairment that is intended to reflect an average reduction in the ability to earn wages in civilian occupations. Veterans' disability ratings range from zero to 100 percent (most severe). Veterans who are unable to maintain gainful employment and who have ratings of at least 60 percent are eligible to be paid at the 100 percent disability rate. Additional allowances are paid to veterans who have disabilities rated 30 percent or higher and who have dependent spouses, children, or parents.

About 50,000 veterans with disability ratings below 30 percent are added to the rolls every year, receiving benefits of between $70 and $188 a month. Federal outlays could be reduced by $2.5 billion during the 2001-2010 period by ending benefits for those low-rated disabilities in future cases.

Making veterans with new disability ratings below 30 percent ineligible for compensation would concentrate spending on the most impaired veterans. Performance in civilian jobs depends less now on physical labor than when the disability ratings were originally set, and improved reconstructive and rehabilitative techniques are now available, so physical impairments rated below 30 percent may not reduce veterans' earnings. Those impairments include conditions such as mild arthritis, moderately flat feet, or amputation of part of a finger—conditions that would not affect the ability of veterans to work in many occupations today.

Veterans' compensation could be viewed, however, as career or lifetime indemnity payments owed to veterans disabled to any degree while serving in the armed forces. Moreover, some disabled veterans—especially older ones who have retired—might find it difficult to increase their working hours or otherwise make up the loss in compensation payments.

700-03 End Future Awards of Veterans' Disability or Death Compensation When a Disability Is Unrelated to Military Duties

	Savings (Millions of dollars) Budget Authority	Outlays
2001	75	69
2002	230	217
2003	393	379
2004	566	552
2005	830	827
2001-2005	2,094	2,044
2001-2010	8,875	8,784

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

700-02 and 700-04

Veterans are eligible for disability compensation if they either receive or aggravate disabilities while on active-duty service. Service-connected disabilities are defined as those resulting from diseases, injuries, or other physical or mental impairments that occurred or were intensified during military service (excluding those resulting from willful misconduct). Disabilities need not be incurred or made worse while performing military duties to be considered service-connected; for example, disabilities incurred while on leave also qualify. The federal government gives death compensation awards to survivors when a service-connected disability is related to the cause of death.

As many as 50 percent of veterans receiving compensation payments may qualify on the basis of injuries or diseases that were neither incurred nor aggravated while performing military duties. Ending disability and death compensation awards in such cases in the future would reduce outlays by almost $8.8 billion over 10 years. Approximately 5 percent of those savings would come from reduced death compensation awards.

This option would make disability compensation of military personnel comparable with that of federal civilian employees under workers' compensation arrangements. However, because military personnel are assigned to places where situations may sometimes be volatile, they have less control than civilians over where they spend their off-duty hours. Therefore, in many cases it might be difficult to determine whether a veteran's disease, injury, or impairment was entirely unrelated to military duties. The formal appeals system of the Department of Veterans Affairs (VA) could be extended to cover rulings specifying that disabling conditions were unrelated to military duties.

Data collected by the VA indicate that more than 200,000 veterans receive a total of $1.3 billion a year in VA compensation payments for diseases that, according to the General Accounting Office (GAO), are generally neither caused nor aggravated by military service. Those diseases include arteriosclerotic heart disease, diabetes mellitus, multiple sclerosis, Hodgkin's disease, chronic obstructive pulmonary disease (including chronic bronchitis and pulmonary emphysema), hemorrhoids, schizophrenia, osteoarthritis, and benign prostatic hypertrophy. Ending new awards only for veterans with those diseases would have a more limited impact than this option because it would not affect all veterans whose compensable disabilities are unrelated to military service. However, it could eliminate compensation for some veterans whose disabilities are not generally service-connected, according to GAO, but whose circumstances constitute an exception to that general conclusion. Such an approach would yield smaller savings than the main option—about $1.4 billion over the 2001-2010 period.

700-04 Eliminate "Sunset" Dates on Certain Provisions for Veterans in the Balanced Budget Act of 1997

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	0	0
2003	764	764
2004	778	778
2005	825	825
2001-2005	2,367	2,367
2001-2010	6,583	6,581

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

700-03, 700-05, and 700-06

Five provisions in law that affect veterans will cease to apply on September 30, 2002—their "sunset" date. As a result, starting in fiscal year 2003, outlays will be higher than if the provisions remained in effect. Those provisions:

- o Protect the monthly benefit for certain pensioners who have no dependents and are eligible for Medicaid coverage for nursing home care, thus lowering pension costs for the Department of Veterans Affairs (VA) but increasing costs for the Medicaid program, which is paid for by the federal and state governments;

- o Authorize the Internal Revenue Service to help the VA verify incomes reported by beneficiaries, for the purpose of establishing eligibility for pensions and benefits;

- o Increase the fees charged for first-time and repeated use of the veterans' home loan program and make the VA more cost-effective in securitizing loans and acquiring property:

- o Authorize the VA to collect from any health insurer that contracts to insure a veteran with service-connected disabilities the reasonable cost of medical care that the VA provides for the treatment of non-service-connected disabilities; and

- o Authorize the VA to charge copayments to certain veterans receiving inpatient and outpatient care and outpatient medication from VA facilities.

This option would make the effects of those provisions permanent by eliminating the sunset date in each case. In addition, it would eliminate the VA's current authority to spend the medical care collections. Beginning in 2003, those collections would revert back to the Treasury. If all five provisions were made permanent and medical receipts were deposited in the Treasury, savings during the 2001-2010 period would total almost $6.6 billion compared with the current level of spending.

The main advantage of this option is that it would convert the temporary savings achieved by those provisions into continuing savings. The main disadvantage is that certain veterans or their insurers would be worse off financially. States would also face higher Medicaid costs because of withdrawn federal funds for nursing home care.

700-05 Extend and Increase Copayments for Outpatient Prescriptions Filled at VA Pharmacies

	Savings (Millions of dollars) Budget Authority	Outlays
2001	0	0
2002	0	0
2003	156	156
2004	211	211
2005	268	268
2001-2005	635	635
2001-2010	2,037	2,037

SPENDING CATEGORY:

Mandatory

RELATED OPTIONS:

050-21 and 700-04

In 1990, the Congress gave the Department of Veterans Affairs (VA) temporary authority to charge copayments for care and services at VA facilities to certain veterans—namely, those with relatively high income and no service-connected disabilities. Copayments for outpatient prescriptions filled at VA pharmacies were set at $2 for a 30-day supply of drugs. The Congress later extended the authority to collect that copayment through 2002 but did not increase the copayment amount, even though the VA's prescription drug expenditures rose by an average of 11 percent per year between 1991 and 1999. The Millennium Health Care and Benefits Act of 1999 has given the VA authority to charge more than $2 for a 30-day supply of drugs, but the department does not yet know how it will implement that authority or what the final copayment will be. (Any increase in revenues would not count as savings since the VA also has authority to spend the money.)

This option would make three sets of changes. First, it would eliminate the provision under which the copayment will expire in 2002 and would extend that payment indefinitely. It would also require the VA to collect copayments in all applicable cases and would remove the department's discretion to waive the copayment. Currently, the VA bills veterans from a central office on the basis of information forwarded by VA pharmacies. Under this option, copayments would be collected by those pharmacies as they dispensed prescriptions. Second, this option would increase the copayment amount by $1 each year until it reached $5 for a 30-day supply. Third, the option would send those collections to the Treasury rather than allowing the VA to spend them, as under current law. Those three actions would take effect in 2003 and would save more than $2 billion through 2010.

Proponents would argue that eventually requiring a $5 copayment for prescription drugs would encourage more prudent consumption and make the VA drug benefit consistent with that of other health care delivery systems, including managed care plans in the private sector.

Opponents, by contrast, would charge that some veterans with multiple chronic illnesses could be overburdened by the higher cost sharing. Even limiting the number of prescriptions subject to copayments in one month could place an undue financial burden on chronically ill veterans and their families, according to critics.

700-06 Increase Beneficiaries' Cost Sharing for Care at VA-Operated Nursing Facilities

	Savings (Millions of dollars) Budget Authority	Outlays
2001	182	182
2002	188	188
2003	194	194
2004	200	200
2005	206	206
2001-2005	970	970
2001-2010	2,097	2,097

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

700-04

Veterans may receive long-term care in nursing homes operated by the Department of Veterans Affairs (VA) depending on the availability of resources. That care is rationed primarily on the basis of service-connected disabilities and income. Under certain conditions, a veteran may receive care at the VA's expense in state-operated or privately run nursing facilities.

The VA may charge copayments to veterans with no service-connected disabilities and high enough income when they receive more than 90 days of care in VA-run nursing homes. In 1998, the copayment rate was equivalent to about $13 a day. A study by the General Accounting Office found that the copayment recovers just 0.1 percent of the costs of providing nursing home care. In contrast, state-operated nursing facilities for veterans and community long-term care facilities that treat veterans have their own copayment policies. As a result, those facilities offset a larger share of their operating expenses than the VA, recovering as much as 43 percent through copayments. (Estate-recovery programs are another way they offset costs.)

This option would authorize the VA to revise its cost-sharing policies to recover more of the cost of providing care in VA nursing facilities. The department would be required to collect a minimum of 10 percent of its operating costs, but it could determine the type of copayments charged and who would be eligible to pay them. For example, it could apply the current copayment to a broader category of veterans or require the veterans who now make copayments to pay more. Recovering 10 percent of the VA's operating costs would save $182 million in 2001 and $2 billion over 10 years. Achieving those savings would require depositing the receipts in the Treasury rather than allowing the VA to retain and spend them. (The Millennium Health Care and Benefits Act of 1999 gave the VA authority to increase copayments charged to the above-mentioned veterans, but the department does not yet know how it will implement that authority or what the structure of copayments will be. Furthermore, any increase in revenues would not count as savings since the VA has authority to spend the money.)

Proponents of this option would argue that veterans in VA nursing facilities are getting a far more generous benefit than similar veterans in non-VA facilities. Because VA-run nursing homes are relatively scarce, veterans lucky enough to be admitted to one receive an unfair advantage over similarly situated veterans. Recovering more of the expense at VA facilities would make that benefit more equitable among veterans and different sites of care.

Opponents of this option would argue that beneficiaries in nursing facilities may be less able to make copayments than beneficiaries receiving other types of care. They would also argue that allowing the VA to charge veterans with service-connected disabilities would be inconsistent with other medical benefits that those veterans receive. The VA could continue to exempt those veterans, but it would have to charge high-income veterans without service-connected disabilities even more to achieve the 10 percent recovery level.

750

Administration of Justice

Budget function 750 covers programs that provide judicial services, law enforcement, and prison operation. The Federal Bureau of Investigation, the Customs Service, the Drug Enforcement Administration, and the federal court system are all supported under this function. CBO estimates that discretionary outlays for function 750 will total $26.8 billion in 2000. Over the past 10 years, this function has experienced steady and often significant annual increases in outlays, reflecting continued concern about drug-related and other crime.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	12.4	12.7	14.3	14.6	15.2	18.3	20.7	22.9	24.8	26.5	26.6
Outlays											
Discretionary	10.1	11.9	14.0	14.7	15.0	16.2	17.6	20.1	22.2	25.0	26.3
Mandatory	-0.1	0.3	0.4	0.3	0.2	0.1	0	0.1	0.7	0.9	0.5
Total	10.0	12.3	14.4	15.0	15.3	16.2	17.5	20.2	22.8	25.9	26.8
Memorandum:											
Annual Percentage Change in Discretionary Outlays		18.3	17.2	4.8	2.6	7.5	8.9	14.3	10.2	12.8	5.1

750-01 Reduce Funding for Law Enforcement Efforts to Control Illegal Drugs

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	2,575	1,681
2002	2,575	2,260
2003	2,575	2,465
2004	2,575	2,527
2005	2,575	2,543
2001-2005	12,873	11,476
2001-2010	25,745	24,324
Relative to WIDI		
2001	2,643	1,730
2002	2,703	2,363
2003	2,766	2,629
2004	2,831	2,763
2005	2,896	2,847
2001-2005	13,838	12,333
2001-2010	29,350	27,804

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

750-02 and 800-05

The federal government currently allocates nearly $18 billion a year for controlling illegal drugs. Of that amount, approximately $3.2 billion is designated for efforts to prevent drugs from entering the United States. Both domestic agencies and the Department of Defense carry out law enforcement efforts to control illegal drugs. Approximately two-fifths of the funds for interdiction and international activities are allocated under the administration of justice budget function. Another one-fourth is allocated to defense-related efforts. (The remainder is split between the transportation and international affairs budget functions.) Eliminating funds for drug interdiction and international activities, which may be relatively less effective than domestic antidrug efforts, would save $1.7 billion in the first year, $11.5 billion over five years, and $24.3 billion over 10 years.

Critics of the funding claim that interdiction and international activities are both more costly and less effective than other antidrug efforts; that no clear proof of their efficacy exists; and that the federal government could drastically reduce the resources devoted to such activities without affecting drug use over the long term. In fact, some sources show that illicit drugs are less expensive and more readily available now than they were before the federal government began trying to control them. Interdiction and international activities do not reduce the demand for drugs and have less impact on the price users pay than state and locally funded efforts. Interdiction and international activities affect producers' costs, which are only a small part of the users' charges. The bulk of those charges are added in the later stages of processing and delivery. (Of course, local and state efforts to control the supply of drugs also face several obstacles: competition among producers and distributors, the large markup from wholesale to retail prices, and the ability of distributors to dilute the drug to maintain an end price that customers can afford.)

Proponents argue that a variety of reasons exist to support interdiction and international activities. Notable successes, including the destruction of major drug trafficking organizations and the large quantities of illegal drugs seized or destroyed, contradict claims of ineffectiveness. In fact, supporters of interdiction and international activities argue that street prices would have been much lower, and the availability of drugs much greater, without extensive funding for criminal justice efforts. Moreover, if the goal of the federal government is to control, and not simply to reduce, the use of illegal drugs, some effort to reduce the flow of drugs into the country will be necessary. Proponents of antidrug activities argue that given the unacceptably high level of drug use, the government should reform allegedly ineffective programs rather than eliminate them. Finally, in cases in which antidrug activities are integrated with other agency functions, cutting back funding for interdiction and international efforts would also disrupt those related activities.

750-02 Reduce Funding for Justice Assistance and Certain Justice-Related Activities

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	696	309
2002	758	558
2003	758	718
2004	758	758
2005	758	758
2001-2005	3,728	3,101
2001-2010	7,518	6,891
Relative to WIDI		
2001	708	313
2002	783	574
2003	797	746
2004	811	799
2005	826	813
2001-2005	3,925	3,245
2001-2010	8,270	7,529

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

750-01 and 800-05

In addition to the law enforcement activities that the Department of Justice carries out directly, it and related government entities provide various types of law enforcement or legal assistance to individuals, community organizations, and state and local law enforcement agencies. That assistance, which will amount to about $1.5 billion in 2000, often takes the form of financial grants to support research, training, and other programs.

This option would consolidate and reform justice assistance programs and reduce the amount spent on them by 20 percent. It would also terminate the Legal Services Corporation and the State Justice Institute. Those cuts can, of course, be considered separately. Taken together, they would save $309 million in 2001, $3.1 billion over five years, and $6.9 billion over 10 years.

The major criticisms of the justice assistance programs are that they do not respond to local concerns and priorities and that they often address problems that are not federal responsibilities. Consolidating grant programs would yield administrative savings, and switching from categorical to block grants would allow grant recipients to focus their efforts on areas of greatest need rather than on problems that, though significant nationally, are less important locally. Similar arguments apply to the Legal Services Corporation, which provides legal assistance to the poor in civil matters. Critics contend that responsibility for such assistance more properly lies with state and local governments. Some critics also charge that the activities of Legal Service lawyers tend to focus on advancing social causes rather than on helping poor people with routine legal problems. (The Congress modified the Legal Services Corporation in 1996, restricting the types of cases and clients it could represent by, for example, prohibiting the corporation's lawyers from representing plaintiffs in class-action suits.) The State Justice Institute, which makes grants for research on criminal justice matters, likewise faces questions of responsibility and jurisdiction. The criticisms leveled against the institute are that much of the research it sponsors is similar to that conducted elsewhere and that in neglecting to publicize the research or cooperate with the courts in instituting reforms and new ideas, it does too little to affect the states' actual administration of justice.

Supporters of funding for justice assistance argue that it is merited on practical grounds. The categorical grant system, they maintain, is working as intended: in certain cases, the problems the grants address have a national scope but might be ignored by states without the incentive of federal funds. Reduced federal spending would, moreover, disproportionately affect those state-run programs that depend heavily on federal funding, such as juvenile justice. In defending the Legal Services Corporation and the State Justice Institute, opponents of this option argue that the federal government has an obligation to provide assistance in areas with scarce support from state and private sources.

800

General Government

Budget function 800 covers the central management and policy responsibilities of both the legislative and executive branches of the federal government. Among the agencies it funds are the General Services Administration and the Internal Revenue Service. CBO estimates that in 2000, outlays for function 800 will total $14.4 billion—most of which is discretionary spending. Over the past 10 years, spending for the function has increased fairly steadily.

Federal Spending, Fiscal Years 1990-2000 (In billions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Estimate 2000
Budget Authority (Discretionary)	11.5	12.2	11.3	11.6	12.1	11.9	11.6	11.8	12.1	13.7	12.6
Outlays											
Discretionary	9.0	10.4	11.0	11.5	11.7	12.4	11.8	12.1	12.0	12.4	13.3
Mandatory	1.6	1.4	2.0	1.5	-0.3	1.6	0.2	0.8	3.7	3.3	1.1
Total	10.6	11.7	13.0	13.1	11.3	14.0	12.0	12.9	15.7	15.8	14.4
Memorandum:											
Annual Percentage Change in Discretionary Outlays		15.3	6.3	4.8	1.1	6.3	-5.1	2.7	-0.5	3.2	6.8

800-01 Restrict Public-Purpose Transfers of Real Property by GSA

	Added Receipts (Millions of dollars)
2001	45
2002	45
2003	45
2004	45
2005	45
2001-2005	225
2001-2010	450

SPENDING CATEGORY:

Mandatory

The General Services Administration (GSA) makes surplus federal buildings, land, and other property available to state and local governments, nonprofit organizations, and others for use as parks, prisons, schools, and airports. The government makes the property available free or at deep discounts. In 1999, according to GSA data, the government donated 90 pieces of property valued at $81 million. For the 1995-1999 period, the value of donations totaled about $500 million. If the government discontinued the program and instead sold surplus property at market value, it could increase offsetting receipts by a total of $450 million over 10 years. (That number represents the net of roughly $500 million in additional receipts less GSA's authority to retain and spend 12 percent of such amounts—or about $50 million over the 10-year period.)

According to supporters of this option, selling surplus property, rather than giving it away, would raise revenue for the government and would ensure, through open competition for assets in the market, that property is put to its most highly valued use. They note that the government already provides abundant direct and indirect assistance to states and localities to support conservation, education, and other public services. They also point out that nonprofit organizations will receive about $30 billion in federal support in tax deductions for charitable contributions in 2000. In addition, the program provides uneven assistance, which favors areas with a heavy federal presence, according to those who would restrict it.

Advocates of transferring surplus property argue that the program provides valuable support to localities, nonprofit organizations, and others struggling to offer useful public services in areas such as education, conservation, and transportation. During periods of fiscal restraint, such programs also offer the government a way to support causes it deems worthy, without having to make appropriations. In addition, advocates argue that transferring surplus property to communities may offset some of the local impact of closing federal installations.

800-02 Eliminate General Fiscal Assistance to the District of Columbia

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	28	28
2002	28	28
2003	28	28
2004	28	28
2005	28	28
2001-2005	140	140
2001-2010	280	280
Relative to WIDI		
2001	28	28
2002	29	29
2003	29	29
2004	30	30
2005	30	30
2001-2005	146	146
2001-2010	306	306

SPENDING CATEGORY:

Discretionary

Under the National Capital Revitalization and Self-Government Improvement Act (Revitalization Act) of 1997, the federal government assumed responsibility for providing certain services to the District of Columbia in exchange for eliminating the annual payment of general assistance to the District. Specifically, the federal government agreed to fund the operations of the District's criminal justice, court, and correctional systems. It also assumed responsibility for paying off more than $5 billion in unfunded liabilities owed by the city to several pension plans, increased the federal share of the city's Medicaid payments, and provided special borrowing authority to the District.

For fiscal year 1998, the Revitalization Act included slightly more than $200 million in assistance for the District that was not related to the obligations specifically assumed by the federal government. For fiscal year 1999, the city received $232 million in such funding, compared with $28 million for fiscal year 2000. The amount for 2000 includes funds for defraying out-of-state tuition costs, providing adoption incentives, and preventing the supply of narcotics. Eliminating such funds would save $280 million over the 2001-2010 period.

One argument for eliminating such funding is that the federal government relieved the District of Columbia government of the cost of a substantial, and increasing, portion of its budget—criminal justice, Medicaid, and pensions. The proposed trade-off for assuming responsibility for those functions was eliminating other assistance, including the annual federal payment. Eliminating assistance would be consistent with that policy. Furthermore, because the District of Columbia's financial situation has recently improved considerably, the city needs less assistance.

One argument against eliminating such funding is that the Constitution gives the Congress responsibility for overseeing the District of Columbia (which the Congress has largely delegated to the city government) and the city still has major problems with its public schools, roadways, and other essential city services. Therefore, opponents of this option argue that the need continues for funding assistance. Moreover, the Congress prevents the District of Columbia from imposing commuter taxes as other cities do. Such taxes are levied on nonresidents who work in a city and benefit from city services. Two of three dollars earned in the District of Columbia are earned by nonresidents. Finally, opponents note that continued assistance is justified because a large portion of city property is exempt from local taxes, including the property owned by the federal government or foreign nations that accounts for over 40 percent of property in the city.

800-03 Eliminate Mandatory Grants to U.S. Territories

	Savings (Millions of dollars) Budget Authority	Outlays
2001	28	2
2002	28	8
2003	28	11
2004	28	16
2005	28	22
2001-2005	140	59
2001-2010	280	197

SPENDING CATEGORY:

Mandatory

As part of the Covenant to Establish a Commonwealth of the Northern Mariana Islands (CNMI), the federal government agreed to provide financial assistance to CNMI, a U.S. territory. During the 1978-1992 period, the federal government provided CNMI with $420 million for operations, economic development, and infrastructure.

After 1992, the financial assistance agreement between the United States and CNMI requires, in the absence of a new agreement, that grants to the Commonwealth continue indefinitely at the 1992 funding amount—$28 million. In 1996, Public Law 104-134 reallocated the $28 million in annual grants among CNMI; the territories of Guam, American Samoa, and the Virgin Islands; and the freely associated states of Micronesia and the Marshall Islands. The reallocation was made, in part, because the government believed that the goals of the original financial assistance agreements had been met and that other areas had a greater need for assistance. Of the $28 million, more than $11 million continues to go to CNMI.

The option and savings assume a new agreement with CNMI. Eliminating the mandatory grants to the U.S. territories and freely associated states would save about $200 million over the 2001-2010 period. Because the territories spend new grants relatively slowly, eliminating the grants would not save much money in the first several years. The Department of the Interior could include additional funding for infrastructure and other purposes as part of its annual appropriation request; however, the territories would no longer be entitled to the $28 million, and requests for additional appropriations for infrastructure grants would compete with all other appropriation requests. For instance, in fiscal year 2000, the Congress appropriated $42 million in assistance to the territories.

Aside from reducing direct spending, eliminating the grants would put assistance for capital needs on equal footing with other assistance to the territories and with similar grants to state and local governments. In addition, some people argue that the reason for providing mandatory assistance to CNMI has ended because its goals have been met. The decision to reallocate the annual funds among the insular areas would seem to support that conclusion. In addition, CNMI has had considerable difficulty developing projects, raising matching funds, and receiving approval from the Department of the Interior, all of which suggests that the goals for which the funding was designed have been met.

Those who would continue the grants argue that the insular areas still have significant needs and that the mandatory grants ensure that funding is available. In addition, CNMI has a growing economy and increasing self-sufficiency, which supporters of this option cite as proof that the federal assistance works. Others argue that any further change in CNMI's funding should be part of a new financial agreement between the United States and CNMI. Otherwise, CNMI could view the unilateral ending of the assistance as a breach of good faith on the part of the U.S. government, which could have political and legal repercussions.

800-04 Require the IRS to Deposit Fees from Installment Agreements in the Treasury as Miscellaneous Receipts

	Savings (Millions of dollars) Budget Authority	Outlays
2001	92	86
2002	94	94
2003	96	96
2004	94	94
2005	96	96
2001-2005	472	466
2001-2010	980	974

SPENDING CATEGORY:

Mandatory

The fiscal year 1996 appropriation act for the Department of the Treasury, the U.S. Postal Service, the Executive Office of the President, and certain independent agencies authorizes the Internal Revenue Service (IRS) to establish new fees and increase existing fees. The act also allows the IRS to retain and spend receipts collected from those fees, up to an annual limit of $119 million. The IRS has used the authority mainly to charge taxpayers a fee for entering into payment plans with the agency. In fiscal year 1999, the IRS collected $88 million and spent $90 million in fee receipts (including $2 million in fees collected before 1999).

Requiring the IRS to deposit those receipts in the Treasury would eliminate the IRS's ability to spend them. That would reduce the IRS's direct spending by nearly $100 million a year, or $974 million over the 2001-2010 period. That estimate assumes that removing the spending authority would not substantially reduce the amount the IRS collects each year from such fees.

An argument for eliminating the IRS's authority to spend the receipts is that processing payment plans with the taxpayers is an administrative function directly related to the IRS's mission—getting citizens to pay the taxes they owe—and for which the agency already receives an annual appropriation. For fiscal year 2000, for instance, the IRS received $8.25 billion in direct appropriations (not counting transfers). That argument may have particular merit because the IRS does not directly use the receipts collected from fees for installment agreements to fund the processing of those agreements. A second argument is that the spending authority could create the incentive for the IRS to unnecessarily encourage taxpayers to pay their taxes in installments. Similarly, it could encourage the agency to seek new and unnecessary fees.

An argument for continuing to allow the IRS to spend the receipts is that given the constraints on total discretionary spending, allowing the IRS to generate and use fee receipts helps ensure that the federal government's main revenue collector has sufficient funding to fulfill its mission. Some people would argue that even an annual decrease of roughly $100 million could negatively affect revenue collection. In addition, eliminating the spending authority could reduce the IRS's incentive to allow, or its ability to provide for, installment payments, thus hurting those taxpayers who would benefit from such arrangements.

800-05 Eliminate Federal Antidrug Advertising

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	185	56
2002	185	148
2003	185	185
2004	185	185
2005	185	185
2001-2005	925	759
2001-2010	1,850	1,684
Relative to WIDI		
2001	188	56
2002	191	151
2003	194	192
2004	198	195
2005	201	198
2001-2005	972	792
2001-2010	2,029	1,833

SPENDING CATEGORY:

Discretionary

RELATED OPTIONS:

750-01 and 750-02

The fiscal year 1998 appropriation act for the Department of the Treasury, the U.S. Postal Service, the Executive Office of the President, and certain independent agencies authorized and provided funding of $195 million to the Office of National Drug Control Policy (ONDCP) for a national antidrug media campaign. The Omnibus Consolidated and Emergency Supplemental Appropriations Act provided $185 million for the program in fiscal year 1999 and authorized $195 million for each of fiscal years 2000 through 2002. Amounts provided to ONDCP can be used to test and evaluate advertising, purchase media time, and evaluate the effects. In addition, the agency must try to get donations from nonfederal sources to finance part of the costs.

For fiscal year 2000, the Treasury and General Government Appropriations Act provided $185 million for the antidrug media program. Thus, eliminating it would save $1.7 billion over the 2001-2010 period, assuming that the Congress will otherwise continue to provide the same level of funding for the program that it provided for fiscal year 2000.

Arguments for terminating funding of the advertising campaign are many. First, solid empirical evidence of media campaigns' effectiveness in either preventing or reducing drug use is lacking. Some analysts claim that media spots do not reduce drug use by minors as effectively as treatment or interdiction. Furthermore, since nonprofit organizations, such as the Partnership for a Drug-Free America, already conduct educational programs about the dangers of drug use, ONDCP's campaign may duplicate private and local efforts. In any event, with more than $300 million in available balances at the start of this year and the authority to solicit and use public donations, ONDCP could continue the media campaign, on a much smaller scale, without an annual appropriation.

Other analysts argue that educating the young about the hazards of drug use is a national responsibility. Some point to the "Just Say No" campaign begun by former First Lady Nancy Reagan in the 1980s as an example of the successful use of the national media to raise young people's awareness of the dangers of drugs. Proponents of the program also argue that the cost of drug abuse to the country is so high that it is worthwhile to maintain a program that reduces drug use even slightly.

800-06 Eliminate the Presidential Election Campaign Fund

	Savings (Millions of dollars) Budget Authority	Outlays
2001	62	0
2002	61	0
2003	60	29
2004	60	226
2005	60	14
2001-2005	303	269
2001-2010	603	596

SPENDING CATEGORY:

Mandatory

During each Presidential election cycle, the federal government distributes money from the Presidential Election Campaign Fund to candidates and political parties who agree to limit their campaign expenditures. All candidates —even those who do not accept public funds—are also bound by federal limits on campaign contributions, established in 1974, that restrict donations by individuals to $1,000.

This option would, after the 2000 election, eliminate the fund and stop the flow of public funds to Presidential candidates and political parties. (Policymakers may, in conjunction with this option, wish to change the rules limiting contributions by individuals, but such changes would not directly affect the budget.) The first savings from this option would not appear until 2003, so total savings over the first five years would be only $269 million, but the total savings through 2010 would be $596 million.

Proponents of this option argue that the current system is unjustified and inefficient. Many critics feel that federal funding has done little to reduce the time or effort candidates spend raising money from private sources. They also charge that candidates have found numerous indirect means of circumventing limits on expenditures, such as "issue advertisements" paid for by parties or special interest groups. They dispute the need to give public funds either to major parties and candidates, which are already well-financed, or to minor parties and candidates, which have little chance of success. Finally, the proportion of taxpayers that choose to earmark a portion of their tax liability for the fund has declined steadily over the past two decades to less than 15 percent, which suggests that the program has little public support.

Opponents of this option believe that the current system limits the influence of special interests and wealthy contributors and allows poorly funded candidates to positively influence the national debate. They argue that public funding has reduced candidates' and parties' dependence on contributions from special interest groups, corporations, and the wealthy. They note that the funds given to candidates from a minor party constitute only a small portion of total public spending on Presidential elections (for the five elections between 1976 and 1992, the amount was less than 2 percent) and allow such candidates to bring public attention to issues that might otherwise be ignored.

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Allowances

The President's budget and the Congressional budget resolution sometimes include amounts in function 920 to reflect proposals that are not clearly specified or that would affect multiple budget functions. Since the Congress actually appropriates money for specific purposes, there are no budget authority or outlay totals for function 920 in historical data. In this volume, function 920 includes options that cut across programs and agencies and would affect multiple functions.

920-01 Eliminate Requirements That Agencies Purchase Alternative-Fuel Vehicles

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	11	8
2002	11	11
2003	11	11
2004	11	11
2005	11	11
2001-2005	55	52
2001-2010	110	107
Relative to WIDI		
2001	11	8
2002	12	11
2003	13	12
2004	14	13
2005	15	14
2001-2005	65	58
2001-2010	152	143

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

920-03

As part of the federal government's efforts on behalf of cleaner air, the Energy Policy Act (EPACT) requires federal agencies to acquire light-duty cars and trucks that can operate using an alternative fuel, such as compressed natural gas, denatured ethanol, or electricity. Beginning in 1999, with certain exceptions, 75 percent of light-duty vehicles acquired for federal fleets in high-density areas must be manufactured or converted to operate as a bi-fuel (gasoline or alternative fuel), flexible-fuel (mixture), or dedicated-fuel (alternative fuel only) vehicle. EPACT annually applies to more than 20,000, or just under half, of new vehicles.

Although agencies have yet to meet any of EPACT's annual targets for acquiring alternative-fuel vehicles (AFVs), they increasingly add AFVs to their fleets. According to the Department of Energy (DOE), to date the government (primarily the United States Postal Service) has ordered, acquired, or converted more than 55,000 AFVs, which can be considerably more expensive to buy and operate than conventional vehicles. For example, the government spends about $4,000 more for a vehicle equipped to operate using compressed natural gas. Eliminating the EPACT requirement would save $107 million in federal transportation costs through 2010.

The estimate of annual savings assumes that agencies will continue under current law to fall short of the 75 percent requirement until the end of the 10-year period. If agencies were to immediately meet current-law targets, increasing their use of AFVs, savings would be greater. The estimated budgetary effect of eliminating the EPACT requirement excludes annual savings to the Postal Service, which is classified as off-budget.

An obvious advantage of eliminating the requirement is that it would reduce transportation costs to the federal government and the taxpayers. In addition, given the annual limits set in law for total discretionary spending, it may no longer be desirable to require agencies to purchase the more expensive AFVs.

A disadvantage of eliminating the requirement is that the federal government would no longer be leading the conversion to AFVs. Such a policy change could discourage similar efforts at the state and local levels. In addition, the development of the AFV market and of less expensive vehicles of that type could slow. Such a result could hurt clean air efforts. However, according to information from the General Services Administration and DOE, many agencies are primarily buying bi-fuel vehicles that comply with EPACT but that do not require the use of alternative fuels.

920-02 Reduce the Number of Political Appointees

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	n.a.	n.a.
2002	n.a.	n.a.
2003	n.a.	n.a.
2004	n.a.	n.a.
2005	n.a.	n.a.
2001-2005	n.a.	n.a.
2001-2010	n.a.	n.a.
Relative to WIDI		
2001	39	37
2002	71	70
2003	75	75
2004	115	113
2005	86	87
2001-2005	386	382
2001-2010	877	872

NOTES: Savings measured from the 2000 funding level adjusted for pay raises and changes in employment.

n.a. = not applicable.

SPENDING CATEGORY:

Discretionary

RELATED CBO PUBLICATION:

Comparing the Pay and Benefits of Federal and Nonfederal Executives (Memorandum), November 1999.

The term "political appointee" generally refers to employees of the federal government who are appointed by the President, some with and some without Senate confirmation, and to certain policy advisers hired at lower levels. For this discussion, the term "political appointee" refers to cabinet secretaries, agency heads, and other Executive Schedule employees at the very top ranks of government; top managers and supervisors who are noncareer members of the Senior Executive Service; and confidential aides and policy advisers referred to as Schedule C employees. The total number of employees in such positions, according to Congressional Budget Office projections, will average about 2,700 over the next 10 years. If the government instead capped the number of political appointees at 2,000, savings over 10 years would total almost $900 million. The current average salary for political appointees, in CBO’s calculations, is estimated to be $89,000.

Reports from several groups, including the National Commission on the Public Service and the Twentieth Century Fund, have called for cuts in the number of political appointees. The National Commission on the Public Service, also known as the Volcker Commission, called for setting a limit similar to the one described here. In addition to the problem of excessive organizational layering, the Volcker Commission described concerns about many appointees' lack of expertise in government operations and programs. In political appointments, the commission noted, political loyalties generally count more than knowledge of government. Moreover, few appointees are in office long enough to acquire the necessary skills and experience to master their job. That lack of experience, according to the commission, means that political appointees in many instances are not effective in carrying out the policies of the President they serve and can disrupt an agency's daily operations. As a result, career managers become frustrated and demoralized, making recruitment and retention difficult in the top ranks of the career civil service.

Critics of reducing the number of political appointees cite the importance of a President's establishing control over the vast bureaucracy by having like-minded individuals and allies strategically situated. Those appointees, critics note, form an important link to the electorate because they help to ensure governmentwide leadership that is consistent with the philosophy of each elected President. Such appointees, moreover, can offer fresh perspectives and innovation. The high rate of turnover among appointees, critics argue, means that those officials make way for someone new before they reach the point of burnout.

920-03 Charge Federal Employees Commercial Rates for Parking

	Added Receipts (Millions of dollars)
2001	110
2002	110
2003	110
2004	110
2005	110
2001-2005	550
2001-2010	1,100

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

920-01

The federal government leases and owns more than 200,000 parking spaces, which it allocates to its employees—in most cases without charge. Requiring federal government employees to pay commercial rates for their parking could yield receipts of $110 million in 2001, $550 million over five years, and $1.1 billion over 10 years.

Federal workers in the largest metropolitan areas would bear the brunt of the new charges. Those in the Washington, D.C., metropolitan area would be affected the most, paying about 75 percent of the total charge. (Federal employees in less commercially developed areas, where charging for parking is uncommon, would not face new parking charges.) Employees who continued to use federally owned or managed parking would, on average, pay about $120 per month; employees who currently use free or heavily subsidized parking could choose alternative means of transportation, such as public transportation or carpooling, to avoid the charge.

Supporters of this option favor charging commercial rates for parking because it would encourage federal employees to use public transportation or carpool. That would reduce the flow of cars into urban areas, cutting down on energy consumption, air pollution, and congestion. By acting as a model employer in this regard, the federal government could more effectively call on others to reduce pollution and energy consumption. In addition, commercial pricing would indicate the demand for parking by federal workers more accurately, enabling the government to allocate spaces to those who valued them the most. Moreover, if commercial rates reduced demand for spaces sufficiently, the government might be able to put the unused spaces to new, higher-valued uses. Finally, some observers argue that the federal government should not provide a valuable commodity, such as parking, free to workers who can afford to pay for it.

Critics of this option argue that by charging for parking, the government would unfairly penalize workers in urban areas who have difficulty obtaining access to alternative transportation or who drive to work for valid personal reasons. Charging for parking would also reduce federal employees' total compensation. In addition, critics note that many private-sector employers provide free parking. Some people also have argued that charging commercial rates would merely re-ration the existing spaces without reducing the number of people who drive to work. According to that view, the spaces would simply be allocated by willingness to pay rather than by rank, seniority, or other factors.

920-04 Impose a Fee on GSE Investment Portfolios

	Savings (Millions of dollars) Budget Authority	Outlays
2001	700	700
2002	700	700
2003	700	700
2004	700	700
2005	700	700
2001-2005	3,500	3,500
2001-2010	7,000	7,000

SPENDING CATEGORY:

Mandatory

RELATED OPTION:

370-10

RELATED CBO PUBLICATIONS:

Assessing the Public Costs and Benefits of Fannie Mae and Freddie Mac (Report), May 1996.

The Federal Home Loan Banks in the Housing Finance System (Report), July 1993.

Controlling the Risks of Government-Sponsored Enterprises (Report), April 1991.

Government-sponsored enterprises (GSEs) are private financial institutions chartered by the federal government to support the flow of funds to agriculture, housing, and higher education. GSEs achieve their public purposes by borrowing on the strength of an implicit federal guarantee of their debt obligations. Investors infer the guarantee from the exemption of GSE securities from the normal protection afforded to investors, Congressional support for the enterprises' public purposes, their exemption from state and local taxes, and the huge volume of their outstanding obligations. The implicit guarantee lowers GSEs' cost of borrowing, thus conveying subsidies that give them a competitive advantage in financial markets.

Before the 1990s, GSEs generally used the money they borrowed to make loans or buy loans made by other lenders. More recently, the three largest GSEs—Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System —have used borrowed funds to acquire enormous portfolios of debt securities. The investments consist mainly of mortgage-backed securities (MBSs) but also include corporate bonds, mortgage revenue bonds, and asset-backed securities. At the end of 1999, the investment portfolios of those three enterprises totaled $745 billion, or 51 percent of their combined assets. A fourth GSE, Farmer Mac, has acquired a smaller investment portfolio. The four enterprises conduct an arbitrage between the market for GSE debt and that for private securities, profiting from the difference between the yields on their investments and their own subsidized cost of funds.

Imposing an annual fee on the four GSEs that earn arbitrage profits that would equal 10 cents for every $100 (10 basis points) of each GSE's holdings of private securities that the enterprise finances with debt would save $700 million in 2001, $3.5 billion over five years, and $7.0 billion through 2010. The fee would reduce the competitive advantage that GSEs have in holding private securities and, at least initially, would reduce the net income of the four that do so; their net income exceeded $8.0 billion (after taxes) in calendar year 1999. The enterprises could avoid the fee by reducing their investment portfolios but would probably not do so because their cost advantage in issuing debt exceeds the fee. The GSEs could also try to recoup lost arbitrage profits by increasing their risk or the prices they charge.

Proponents of imposing the fee argue that the affected GSEs could still achieve their public missions with the fee. The Congress never intended the GSEs to crowd other investors out of the markets for MBSs and other debt securities. The profits of each enterprise subject to the fee would remain above competitive levels (except for Farmer Mac, which earns low profits now). The three housing GSEs would still increase their purchases of MBSs when prices fell, thereby stabilizing that market. Critics counter that greater risk taking by the four enterprises could increase the government's risk exposure. Federal risk-based capital requirements and regulatory examinations, if effective, would limit the amount of any increase in the GSEs' risk borne by the government. Fannie Mae and Freddie Mac could possibly raise the interest rates on new mortgages they bought, but competition from wholly private firms and between those two GSEs would limit their ability to do so.

920-05 Repeal the Service Contract Act

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	960	915
2002	960	960
2003	960	960
2004	960	960
2005	960	960
2001-2005	4,800	4,755
2001-2010	9,600	9,555
Relative to WIDI		
2001	985	935
2002	1,005	1,005
2003	1,025	1,025
2004	1,050	1,050
2005	1,070	1,070
2001-2005	5,135	5,085
2001-2010	10,860	10,800

SPENDING CATEGORY:

Discretionary

The McNamara-O'Hara Service Contract Act of 1965 (SCA) sets basic labor standards for employees working on government contracts whose main purpose is to furnish labor, such as laundry, custodial, and guard services. Contractors covered by the act generally must provide those employees with wages and fringe benefits that at least equal those prevailing in the contractors' locality or those specified by a collective bargaining agreement of the previous contractor. The Department of Labor measures prevailing wages in an area according to the specific wages and benefits earned by at least 50 percent of workers in a particular type of job or by the average of the wages and benefits paid to workers in that type of job. The provision about collective bargaining agreements applies to successor contractors, regardless of whether their employees are covered by such an agreement.

In 1999, the SCA covered approximately 28,000 contracts valued at about $30 billion. The Department of Defense accounted for about half of that dollar value.

The cost of services procured by the federal government could be reduced by repealing the SCA. Repealing the act would reduce outlays by about $900 million in 2001 and by about $9.6 billion over the 2001-2010 period, provided that federal agency appropriations were reduced to reflect the anticipated reduction in costs.

Federal procurement costs would fall because repealing the SCA would promote greater competition among bidders, although the precise magnitude of the savings is difficult to measure. Repealing the SCA would give contractors added flexibility that could allow them to reduce the costs of providing services. Opponents of this option are concerned, however, that it would allow bidders to undermine existing collective bargaining agreements. In addition, repealing the SCA would reduce the compensation of workers in some firms that provide services to the government, which opponents argue could reduce the quality of such services.

920-06-A Repeal the Davis-Bacon Act

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	630	265
2002	630	710
2003	630	975
2004	630	1,105
2005	630	1,190
2001-2005	3,150	4,245
2001-2010	6,300	10,450
Relative to WIDI		
2001	640	265
2002	655	715
2003	665	995
2004	680	1,145
2005	695	1,250
2001-2005	3,335	4,370
2001-2010	7,020	11,220

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

920-06-B

Since 1935, the Davis-Bacon Act has required that "prevailing wages" be paid on all federally funded or federally assisted construction projects with contracts of $2,000 or more. The Department of Labor measures prevailing wages in an area according to the specific wages and benefits earned by at least 50 percent of workers in a particular type of job or the average of the wages and benefits paid to workers in that type of job. Those procedures, as well as the classifications of workers who receive prevailing wages, favor union wage rates in some cases.

In 1999, approximately $57 billion in federal discretionary funds was authorized for construction projects covered by the Davis-Bacon Act. Fifty-four percent of that amount went to transportation projects, 13 percent went to the Department of Housing and Urban Development and other community and regional development projects, and 14 percent went to the Department of Defense. (Most of the spending authority for transportation projects is controlled by limitations on obligations rather than by budget authority.)

The federal government could reduce outlays for construction by repealing the Davis-Bacon Act. Doing so would reduce discretionary outlays by about $265 million in 2001 and $10.5 billion over the 2001-2010 period, provided that federal agency appropriations were reduced to reflect the anticipated reduction in costs. Mandatory spending would fall by about $10 million in 2001 and $255 million over the 10-year period.

Repealing the Davis-Bacon Act would allow the federal government to spend less on construction, although the precise effect of repealing the act on contractors' costs is difficult to measure. In addition, it would probably increase the opportunities for employment that federal projects would offer less skilled workers.

However, such a change would lower the earnings of some construction workers. In addition, opponents of this option argue that eliminating Davis-Bacon requirements could jeopardize the quality of federally funded or federally assisted construction projects. They contend that by requiring firms to pay at least the locally prevailing wage, the people they hire are more likely to be able workers, resulting in fewer defects in the finished projects and more timely completion.

920-06-B Raise the Threshold for Coverage Under the Davis-Bacon Act

	Savings (Millions of dollars) Budget Authority	Outlays
Relative to WODI		
2001	205	50
2002	205	155
2003	205	215
2004	205	245
2005	205	260
2001-2005	1,025	925
2001-2010	2,010	2,250
Relative to WIDI		
2001	210	50
2002	215	160
2003	220	220
2004	225	250
2005	230	270
2001-2005	1,100	950
2001-2010	2,310	2,425

SPENDING CATEGORY:

Discretionary

RELATED OPTION:

920-06-A

An alternative to repealing the Davis-Bacon Act (see option 920-06-A) would be to raise the threshold for determining which projects are covered by the act. In recent years, several bills have been introduced that would raise the threshold by various amounts. Raising it from $2,000 to $1 million would save about $50 million in 2001 and about $2.3 billion in discretionary outlays over the 2001-2010 period, provided that federal agency appropriations were reduced to reflect the anticipated reduction in costs. In addition, it would save $1 million in 2001 and $30 million over the 10-year period in mandatory spending. Although this option would save only about one-fifth of the amount that would be saved by repealing Davis-Bacon, the option would reduce firms' and the government's administrative burden by restricting coverage to the largest contracts.

As with repealing the Davis-Bacon Act, raising the threshold would allow the federal government to spend less on construction, although the precise effect of raising the threshold on contractors' costs is difficult to measure. In addition, it would probably increase the opportunities for employment that federal projects would offer less skilled workers.

However, such a change would lower the earnings of some construction workers. In addition, opponents of this option argue that raising the threshold could jeopardize the quality of federally funded or federally assisted construction projects. They contend that by requiring firms to pay at least the locally prevailing wage, the people they hire are more likely to be able workers, resulting in fewer defects in the finished projects and more timely completion.